Retirement Planning

Financial Capability

Strategy for the UK

Retirement Planning

- The entire retirement planning landscape has undergone significant change in the last decade, and this seems likely to continue.

- Given the evolving environment of pensions and retirement planning, developing an evidence base to understand people's financial capability for this area is a key priority for the Strategy.

- Key elements of the Strategy will also include improving access to and people's understanding of guidance and regulated financial advice and piloting interventions with selected employers to help their employees see the need to plan and increase their retirement savings.

Introduction

Retirement planning raises a very particular set of financial capability issues that affect young adults, working-age people and older people in retirement. The Strategy has developed a distinct action plan focused on retirement planning to reflect the unique challenges people face in planning for retirement, making decisions about retirement income, and managing retirement savings throughout life.

This part of the Strategy applies to the whole of the UK.

Evidence and key issues

This is an area that has undergone significant change, which looks set to continue in the short and medium term. Automatic enrolment into workplace pensions started in 2012. April 2015 saw the introduction of the biggest reform of the retirement system which gives people freedom over how to use their pension savings and the introduction of the Pension Wise guidance service.

The pension reforms are continuing with the introduction of the new state pension from April 2016 and the secondary annuities market in 2017. Changes in areas of guidance and financial advice, pensions tax relief, pension transfers and charges are also likely to affect financial capability. These changes represent a significant cultural shift in the way individuals save, plan for their retirement and manage their retirement savings. Retirement is a key focus for the Strategy as people's behaviours change in response to the new reality.

The Office of Fair Trading (OFT's) market study into defined-contribution workplace pensions stated that "the buyer side of the DC workplace pensions market is one of the weakest that the OFT has analysed in recent years".[101] People find it hard to engage with or understand their pensions due to the high level of product complexity.

Financial capability and retirement

People preparing for later life will need improved financial capability and support to make informed choices when building and then turning investments and savings into an income to fund retirement.

The evidence base for this area is varied and there is no single definitive source of data on financial capability in the area of retirement planning. The current Financial Capability Survey contains a relatively small set of questions around pensions and retirement. Developing the financial capability evidence base, including providing a baseline for financial capability around retirement planning is a significant priority for the Strategy. It requires a different set of capabilities than being able to manage money day to day. It is imperative to gain insight into people's ability to save and manage their long-term savings.

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[101] Defined contribution workplace pension market study (Office of Fair Trading, September 2013 revised February 2014)

Under-saving

The Strategy will focus on people who are investing or saving inadequately for retirement.

The Financial Capability Survey indicates that 46% of working-age people say they are currently paying into a pension, 49% are not and 4% don't know. Automatic enrolment will increase the number of people saving into pensions but it is widely acknowledged that automatic enrolment levels at 8% total minimum contribution are not going to provide adequate savings for most people.[102] DWP analyses give a sense of the scale of the working-age population who are currently saving/planning inadequately for retirement (under-savers).[103]

This analysis suggests almost 12 million people are under-saving, with most of those people (three-quarters) earning between £22,700 and £52,000 per annum.[104]

Table 1: Undersavers by Pensions Commission income band

Pensions Commission income band	Number of undersavers	As proportion of Pensions Commission band	As proportion of all undersavers
Band 1 (under £12,300)	0.2m	7%	1%
Band 2 (£12,300 to £22,700)	1.9m	23%	16%
Band 3 (£22,700 to 32,500)	4.2m	52%	35%
Band 4 (£32,500 to £52,000)	4.6m	62%	38%
Band 5 (Over £52,000)	1.1m	67%	10%
Total	11.9m	43%	100%

Thanks to policies on automatic enrolment, the single-tier state pension and the pension triple lock, projections are that 93% of those in the lowest income band (under £12,300 per annum) will achieve adequate retirement income.

Mild under-savers, i.e. people already within 20% of achieving adequate retirement income, could improve their situation by making relatively achievable changes to their behaviour – choosing to work longer, saving more while in work, or saving more than the minimum.

Yet modest under-savers – those between 50%-80% of achieving target retirement income – could benefit from more support, whether that be to increase their pension saving or to better financial planning of their assets and liabilities during their working lives.

Research initiatives are needed to test and pilot different approaches to nudge people into saving more into their pensions, which would benefit the vast majority of people who are currently under-saving.

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[102] The total minimum contribution is currently set at 2%, from October 2017 this will rise to 5%, from October 2018 it will rise to 8%.
[103] *Framework for the analysis of future pension incomes* (DWP, 2013); Scenario analysis of future pension incomes (DWP, 2014)
[104] The Pensions Commission was a public body set up to review the regime for UK pensions and long-term savings. The Commission is now disbanded. Its reports are often referred to as the Turner Reports.

Retirement income decisions

Under-saving is only part of the story. Even the most financially capable people can struggle to understand the benefits and risks of different product choices and to make informed decisions about retirement planning, especially all of the new choices provided by the pension freedoms.

Prior to the changes announced in the 2014 Budget, the FCA estimated that people lose out on around £115-£230 million a year by not making the best choices about how to turn retirement savings into income.[105] In a National Employment Savings Trust (NEST)[106] survey, only 40% of respondents under 40 felt they had an idea of what kind of income they might need in retirement; and this figure rose to only 57% of people over 40.[107]

It is too early to understand fully the behaviour and decisions that people are making about their pension pots. Early reports from the FCA indicate that 204,581 pension policies have been accessed within the three months following the pension reforms. 120,688 individuals have accessed some form of cash withdrawal with 71,455 individuals using some form of income drawdown and 12,418 individuals buying an annuity.[108]

The Financial Capability Survey shows that whilst there are a wide range of sources people intend to use to fund their retirement, the state pension and personal or workplace pensions are by far the most common.

Base: All who are not retired	Total (2849)	18-24s (744)	Working age (2786)
	%	%	%
State retirement pension	49	22	48
Personal or workplace pension	42	29	44
Your partner/spouse's personal/workplace pension	14	6	15
Savings or investments	32	34	32
Downsizing your home or equity release	10	4	10
Buy-to-let or other income from a property which is not your main home	6	4	6
Inheritance that you expect to receive	12	10	12
Inheritance that you have already received	3	4	3
Earnings from part-time/freelance work	12	10	12
Something else (please specify)	1	1	1
Don't know	18	37	19
Prefer not to say	4	4	4
NET: Any pension	**66**	**41**	**65**
NET: Any inheritance	**13**	**14**	**13**

[105] *Freedom and Choice in Pensions* (HM Treasury, 2014)
[106] NEST is a pension scheme set up by the government mainly to help employers with automatic enrolment.
[107] *Taking the temperature of automatic enrolment* (NEST, 2014, p. 25)
[108] Pension freedoms data collection exercise: analysis and findings (FCA, 2015)

There is a role for the Strategy to create a comprehensive literature review to co-ordinate the various reports and research that are emerging. This will enable the sector to identify key areas for further research or highlight synergies that may be exploited across different projects.

Changing policy landscape

The pensions policy landscape is continuing to evolve. The Work and Pensions Committee is currently undertaking an inquiry to "examine whether people are adequately supported in making good, informed decisions about their retirement savings in light of the changes on access to pensions and pension drawdown introduced in April 2015".[109]

The government has also issued consultations on pensions tax relief[110] and pension transfers and exit charges.[111] The outcome of these consultations may result in new legislation that may have an impact on people's behaviour in the retirement market.

Improving access to pension information

Pension language and jargon make the market difficult for people to navigate. The Department for Work and Pensions and NEST have created language guides to support consumer understanding for the introduction of automatic enrolment.[112] The Association of British Insurers (ABI) are also starting a cross sector group to build on the work of DWP and NEST in light of the new pension freedoms.

The FCA's retirement income market study is testing ways to improve how consumer information is presented to help people to make decisions about their retirement income and the type of information they receive in the run up to their retirement.[113] All of these initiatives need to be co-ordinated to reach people and improve their retirement journey.

The ease with which people can access their information is important to address when improving financial capability. There are currently a number of digital initiatives aimed at addressing this.

● 'Pensions Dashboard' – The FCA would like to see the development of a pensions dashboard for the UK which would allow individuals to see all of their lifetime pension savings including their State Pension.[114]

● Open Identity Exchange (OIX) 'Pension Finder' Tool – This project developed a pension finder prototype to examine the hypothesis that individuals will take action and make informed choices when they have information about their pension savings.[115]

● The Savings and Investment Policy Project (TSIP) 'Digital Passport' – This type of digital initiative would verify individuals' identity and allow savers to open new products and transfer money between organisations more easily, through making information more accessible.[116]

As a result of the significant developments in retirement planning there are many initiatives being conducted to develop our understanding and improve the landscape for individuals. The Strategy offers the ability to co-ordinate initiatives to maximise the benefit for individuals and leverage resources across organisations, and avoid duplication.

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[109] Pension freedom guidance and advice inquiry (Work and Pensions Committee, 2015)

[110] Strengthening the incentive to save: a consultation on pensions tax relief (HMT, July 2015)

[111] Pension transfers and early exit charges (HMT, July 2015)

[112] Automatic enrolment and pensions language guide (DWP, 2011) and Phrasebook v 2 (NEST, 2011)

[113] Retirement income market study: final report – confirmed findings and remedies (FCA, March 2015)

[114] Ibid., Remedy 4 page 52

[115] The Pensions Finder tool: a discovery project white paper (Open Identity Exchange (OIX), June 2015)

[116] Press release (Tax Incentivised Savings Association (TISA, December 2014)

Priority areas for action

The identified priority areas for action are:

Priority 1: Developing the evidence base to understand people's financial capability for retirement planning

The capabilities required to plan for retirement are very different from those needed to manage money well day to day. There is currently no definitive evidence base – it is vital to gain insight into people's ability to save and manage their long-term savings.

Priority 2: Improving access to pension information

Navigating the complex pensions market can be difficult for people, so one area where the Strategy will focus will be improving the ease and accessibility of pension information.

Priority 3: Leading the co-ordination of collaborative efforts to improve the consumer retirement journey

The retirement journey can and should be improved to help people build their financial capability around making decisions about what they do with their pension pots.

Priority 4: Improving access to, and consumer understanding of, guidance and regulated financial advice

Understanding the value of, and knowing how to access guidance and advice on saving and planning for later life is an important element of building people's financial capability.

Priority 5: Piloting programmes to nudge people to increase their pension contributions during their working lives

The majority of people are not saving enough for their retirement. The Strategy will seek to pilot different interventions with some employers and their employees to establish what works in terms of helping people increase their retirement savings.

Action Plan

This section outlines the proposed actions to address the priority areas outlined above. The Retirement Planning Steering Group will further refine, prioritise, and evolve the action plan, which will be published and updated on the Financial Capability website.

1 **Developing the evidence base to understand people's financial capability for retirement planning**

  a. Create a retirement planning financial capability survey to provide a better understanding of key barriers and enablers to retirement planning.

2 **Priority 2: Improving access to pension information**

  a. Co-ordinate digital initiatives focused on improving the ease and accessibility of pension information for consumers. This activity will provide a platform to create synergies across digital projects and use resources most effectively across the sector. At the time of publishing, projects that could be included are the *Pensions Dashboard, Open Identity Exchange (OIX) Pension Finder Tool* and the *Digital Passport*.

  b. Build an enhanced retirement income planning tool that allows people to develop different retirement income scenarios.

3 **Leading the co-ordination of collaborative efforts to improve the consumer retirement journey**

  a. Removing barriers such as unaligned hand-offs between organisations. Agree common tools and protocols to help to improve the consistency of the customer experience as individuals move between different organisations on their customer journey.

  b. Champion the use of consistent consumer language and messaging for people's pension savings and retirement income choices:

  ▶ the *Association of British Insurers* is leading a cross-sector group to create a common protocol for pensions language.

  ▶ Incorporate the recommendations of the remedies from the *FCA Retirement Market income study* to improve the way information is framed to consumers in making their decisions about retirement income.

4 **Improving access to, and consumer understanding of, guidance and regulated financial advice**

  a. Help consumers to understand the value of both guidance and regulated financial advice, and the appropriate times to access each service.

  b. Take forward the recommendations from the *FCA/HMT Financial Advice Market Review*, *HMT*'s guidance review and the *Work and Pensions Committee* to translate these for consumers.

5 | **Testing and piloting programmes aiming to nudge people to increase their pension contributions during their working lives**

   a. Create interventions to pilot with some employers and their employees to help people see the need to and increase their retirement savings.

   b. Develop easily understood 'rules of thumb' on retirement saving that are capable of being taken up population-wide.

   c. Develop tools to enable people to co-ordinate their retirement saving with other aspects of financial management such as budgeting, debt management and debt repayment.