The Money Charity Response – DWP Consultation on Simpler Annual Benefit Statements for Defined Contribution Pension Schemes (June 2021)

The Money Charity is a Financial Capability charity whose vision is to empower people across the UK to build the skills, knowledge, attitudes and behaviours to make the most of their money throughout their lives, helping them achieve their goals and live a happier, more positive life as a result.[1]

We welcome the opportunity to respond to the Department for Work and Pensions' consultation on simpler annual pension statements for Defined Contribution pensions schemes used for Auto-Enrolment.

In this response, we set out our Key Points, make some general remarks on the issue then answer the questions posed in the Consultation Paper.

[1] See box on back page.

Key Points

1. We support the proposal to introduce simplified annual pension statements in standard form, which we plan to use educationally in the pension workshops we run.

2. Referring to the DWP's comments on fragmentation and inconsistency of standards in the UK pension system, we urge DWP to seek ways to move the UK toward a system where each pension saver has a single account that follows them through life. This would automatically remove the problem of lost pensions and inconsistent information. We suggest UK policy makers look at successful schemes of this type overseas such as the Singapore Provident Fund and KiwiSaver in New Zealand and see if more features of these schemes can be introduced in the UK.

3. We propose three amendments to the draft Statutory Guidance, relating to the presentation of costs and charges, the presentation of investment returns and the adoption of inclusive design for testing of user-friendly statements.

4. We propose seven amendments to the illustrative statement template, as set out in answer to question 3 below.

5. We agree that the new statements should be introduced in 2022, with as few firms as possible taking advantage of the transitional regulations to delay the new statement until 2023.

General remarks

One of the products delivered by The Money Charity is pension workshops for employees. These are organised via participating employers and take place in employer time or over lunch breaks. Typically, they are a series of one-hour sessions, which cover the pension basics and discuss how to make pension plans in terms of the lifestyle choices people wish to make. We use an interactive style, based on active learning methods, as these have been proven to have the best educational outcomes.[2]

One thing we have learned from this work is people's low level of awareness of how the pension system works and their individual pension entitlements. People often have little idea of what they will get even from the State Pension, let alone the accumulation of their various occupational pensions. A key activity in our workshops is taking participants through a "pension calculator" (we use one available for free from a large pension company) to show exactly what their retirement income trajectory looks like. People often

[2] The Money Charity 2021, *Personal Financial Education: Evidence of Success from Recent Studies.* Available at: https://themoneycharity.org.uk/financial-education-3-5-times-effective-previously-thought/

realise at this point that they are heading for a much lower retirement income than they hoped or planned for. We then discuss options for boosting retirement income, principally via increased savings.

For these reasons we support the introduction of a simpler annual pension statement. We comment on this further in our answers to the consultation questions.

First, though, we would like to make a general point for DWP to consider. The Consultation Paper notes that:

> "Pension savers are increasingly likely to be members of more than one workplace pension scheme. Therefore, they receive multiple annual statements which are inconsistent in design, length and approach, presenting an additional barrier to engagement and understanding."[3]

We strongly agree with this observation. A basic feature of the UK pension system, as it has evolved, is fragmentation. Over a working career, people typically belong either to no pension scheme at all (those who fall outside of auto-enrolment) or to multiple pension schemes with different characteristics, run by different providers. Sometimes the names of the schemes change because pension portfolios are sold by one provider to another, adding to the confusion. Many accounts get "lost" because scheme members change their addresses, employers and/or their names, and the industry seems not to put enough effort into tracking down lost account holders.

Fragmentation is inimical to engagement. Inconsistency in presentation is part of the problem, but fragmentation is the underlying issue. The Pensions Dashboard project has been designed, in part, to address this, but may not provide a complete solution because of data matching and related technical issues.

In our view, UK policy makers should explore solutions that bring greater coherence to the design of the UK pension system, looking at positive overseas examples such as the Singapore Provident Fund or KiwiSaver in New Zealand. A key feature of these schemes is that the account is attached to the scheme member, not to their employer or their pension fund(s). A saver has an account in their own name, which follows them through their life. Different employers contribute to this account during the time that the scheme member works for them. The money saved is managed by the pension fund industry, with safeguards to make sure that costs are reasonable and investments sound.

The evidence from Singapore, New Zealand and other places with such schemes shows that scheme members develop a much stronger sense of ownership of an account in their own name, which follows them wherever they go. They can see the accumulation of their funds over the course of their career and the way that state support and compound

[3] Consultation Paper, page 5.

earnings contribute to the growth of their savings. The annual report is automatically standard because people have a single retirement account. In fact, people can check the state of their account any time online, so have the opportunity for continual engagement and learning.

As Jean-Baptiste Andrieux commented about the French pension system[4] in a recent article in *Money Marketing* (4 June 2021):

> "I believe [the French pension system] is much simpler and more understandable for the average person in comparison to the UK system. There is no such thing as lost or spread pension pots, there are no dilemmas between annuities or drawdown, etc.
>
> It is also much more predictable in terms of income an individual will receive after retiring."[5]

In our view, UK policy makers should look closely at these examples and seek to move the UK system in this direction. For example, it would be beneficial to have a simpler system of pension consolidation, possibly with default features, so that a scheme member could choose to have their pension follow them through their career, or for a new employer to continue paying into the scheme they already belonged to. Consideration would need to be given to the safety checks that would accompany such a default, including controls on costs and charges. A greater degree of unification would give us a more member-centred pension system, which we believe to be a desirable policy outcome.

Answers to consultation questions

Q1: Do you have any comments on whether the draft regulations achieve our policy intention in relation to requiring use of a statement of one double-sided sheet of A4 paper for use by certain defined contribution pension schemes used for automatic enrolment (as defined in the draft regulations)?

We support the intention to produce a standard statement with a maximum length of one double-sided sheet of A4 paper. The draft regulation appended to the consultation paper

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[4] The occupational pension system in France is based on DC accounts in the name of the pension saver, with savers accumulating "points" which, multiplied by point value, give an easy-to-understand pension entitlement.

[5] Available at: https://www.moneymarketing.co.uk/analysis/weekend-essay-how-do-the-french-and-british-pension-systems-differ/?eea=K0JnK0tXU3hWeWxhWXBWSzl1Snl5dU0yRDRoQlVVRjhJODFEM25BNmVvVT0=&n_hash=1897&utm_source=e-shot&utm_medium=email&utm_campaign=MM-967-(Edi)-LatestNews-%231897

appears to achieve this intent, however, as a small charity we do not have the legal resources to comment in detail on the wording of the regulation.

Q2: Do you have any comments on the draft statutory guidance in terms of content or clarity?

We support the overall approach of the draft statutory guidance, setting out a clear presentation of scheme members' savings during the year, the value of their account at the end of the year, the forecast of their retirement income, scenarios for improving retirement income and the accessibility provisions of paragraphs 41-46. Based on our pension workshop experience, enabling people to see how to improve their retirement income is particularly important.

We would like to see improvements to the guidance in three areas:

Presentation of Costs and Charges

The current draft is weak regarding costs and charges, seeming to make this aspect of the statement voluntary and, at the option of the pension provider, accessible via a web link rather than as part of the standard statement. Costs and charges are important for two reasons. First, they can significantly affect the accumulation of pension savings. Second, they are part of the competitiveness of pension schemes. If someone finds they are in a high-cost scheme where charges are eating investment returns, they may wish to switch to a scheme with lower charges and/or a different investment approach that has lower overhead costs. This applies, too, when people have multiple deferred pensions. The ability to see all costs and charges may be an important part of decisions on pension consolidation.

In our view, a statement of costs and charges should be a compulsory part of the presentation.

It is important that costs and charges not be fudged by assigning costs or charges to other items in the presentation (for example, "investment returns net of costs"). The costs and charges line should include all management fees and trading costs. The inclusion of trading costs is important because it will show if a fund is engaging in excessive churn.

Investment Returns

Investment returns are a key part of accumulating pension savings (indeed one of the key arguments employed to encourage pension engagement) but the draft guidance is vague on how these should be presented. In some years, investment returns will be negative, which will disrupt scheme members' understanding of their pension savings unless made clear. In our view, investment returns should be shown clearly in the annual statement, as happens, for example, on retail investor platforms.

In simple terms, the movement in value of a pension account over the year is as follows:

Balance at beginning of year

Plus member contributions

Plus other contributions (employer, state, transfers)

Plus or minus investment returns

Minus costs and charges

Balance at end of year

If the statement is presented in this way, it will be complete and educational.

Inclusive Design

We agree with the design principles set out in the draft statutory guidance, but we think a commitment to inclusive design should be added. A key aspect of inclusive design is the method used to arrive at the final design: **designs should be tested with the target audience before being finally decided**. It is well known in the design profession that user testing reveals difficulties and issues not foreseen in prototype designs. It is important that providers make sure their presentations are understood by a large proportion of the target audience. If initial designs are not understood, then refinements should be made until a better design is achieved.

Q3: Do you have any comments on the illustrative statement template in terms of content or clarity?

We agree with the broad format of the illustrative statement, which we envisage using in our pension workshops as an educational tool.

However, there are some amendments to the detail of the statement we would like to see:

Section 2

Amend the presentation labelled "This Year" as shown by the deletions and underlining below:

You have saved into your Pension Plan	£XXX
Your employer has added	£XXX
The government has added – through tax relief (if applicable)	£XXX

Your investments have increased or decreased in value ~~(after charges if applicable)~~	£XXX
Costs and charges have been deducted from your pension plan ~~(if available)~~	£XXX
You have transferred money from another pension scheme	£XXX
The total value of your Pension Plan on [end of year date] is	£XXX
If you asked to transfer your money to another pension scheme on [date], we would have transferred	£XXX

Taking the proposed amendments to Section 2 in order:

The phrase "after charges if applicable" is an invitation to hide charges in investment returns and should, in our view, be deleted. All charges and costs should be shown in the charges and costs line.

Disclosure of costs and charges should be obligatory, so the bracketed words "if available" should be removed.

A line needs to be added, which says "The total value of your Pension Plan at [year end]". This is to complete the sum of the lines above.

It may be intended that the sum and the transfer value are the same amount, but in our view, these are two different ideas which are confusing if merged. The sum needs to be set out first, prior to any discussion of transfers or transfer values.

Amend the following sentence as shown:

> Find out about costs and charges that apply to your Pension Plan, ~~why we think they are good value for money~~ and how they might affect the value of your Pension Plan over time at ***[web link]***

It is not necessarily true that the costs and charges associated with a particular pension plan are good value for money, so this should not be included as an assumption. It is also not necessarily true that the provider thinks that the costs and charges are good value for money. They might be frustrated that the management of some investments is too expensive, or they may themselves be pricing according to "what the market will bear" rather than at the most economic level. So, there are several reasons for not including this as an assumption. Indeed, many observers of the pensions industry might view the deleted phrase as magical thinking.

The Financial Conduct Authority has recently confirmed the problematic nature of a "value for money" assumption, noting in its consultation paper on a New Consumer Duty that:

> “We have seen complex savings and investment products where the complexity disguises high risks, high costs or poor prospects of the product delivering a return commensurate with the risks and costs.”[6]

In our view, it would be unwise to include in the illustrative statement an assumption contrary to the evidence described by the Financial Conduct Authority.

As Government, FCA, Bank of England and the industry are moving towards compulsory environmental reporting, consideration should be given to strengthening the reference in the illustrative statement to climate change reporting, for example amending the following sentence as shown:

> **Find out more about your Pension Plan on our website *[web link*]**
> Here you can find out*:* how money goes in and out of your Pension Plan; how to transfer money in from another pension scheme and how we invest your money, <u>including the impact of your pension plan investments on the environment and climate change</u> – *This should include pooled funds ~~and where applicable information on climate change.~~*

Things are moving fast in the relationship between business and the environment (for example, the recent shareholder votes for pro-environment Exxon directors and for emission reductions by Chevron, and the court decision in the Netherlands against Shell’s emissions plan) so it makes sense for the pension statement to include firmer reference to climate change and other environmental impacts.

In this context we have observed an upsurge in interest among young investors and savers in ESG investing, so we view this very much as the trend of the future. Including ESG reporting would be an additional tool for engaging young people in pension saving.

Section 3

The box diagram makes an assumption which we think should be spelled out at the beginning of this section:

“If you continue saving into your pension at the current rate…”

Section 4

The phrase, “*Consideration from other sources including the State Pension and other pension pots”* is not clear.

[6] Financial Conduct Authority 2021, CP 21/13 *A New Consumer Duty*, page 32.

We think what is intended is, “How to increase income from other sources such as the State Pension and other pension pots.” If this is what is intended, we suggest that the phrase be amended accordingly.

Q4: Do you have any comments on the timetable in which it is proposed the regulations will come into effect, including the transitional provisions in regulation 3?

We agree with the regulations coming into force in 2022 but think that care needs to be taken around the wording of the transitional provisions. There is a risk these could operate to postpone new statements until 2023. We suggest that DWP look carefully at the reporting timetable of pension schemes and work with the industry to make sure that the majority adopt the new format in 2022. Using the old format 2022 should be the exception rather than the rule.

Firms have been alerted that this is coming and have plenty of time to get prepared for 2023 reporting.

The Money Charity is the UK's Financial Capability charity providing education, information, advice and guidance to all.

We believe that everyone achieves Financial Wellbeing by managing money well. We empower people across the UK to build the skills, knowledge, attitudes and behaviours to make the most of their money throughout their lives, helping them achieve their goals and live a happier, more positive life as a result.

We do this by developing and delivering products and services which provide education, information and advice on money matters for those in the workplace, in our communities, and in education, as well as through influencing and supporting others to promote Financial Capability and Financial Wellbeing through consultancy, policy, research and media work.

We have a 'can-do' attitude, finding solutions to meet the needs of our clients, partners, funders and stakeholders.

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