Wake up to freedoms
Providing flexibility and choice for pension scheme members

An introduction to a series of papers commissioned by LV= Corporate Solutions
Introduction from Steve Lewis

It’s now almost two and a half years since George Osborne made his famous budget announcement introducing freedom and choice in pensions and from that moment the retirement solutions world changed forever.

As the new legislation was primarily aimed at Defined Contribution (DC) schemes, the impact on the Defined Benefit (DB) market was blurred for a short period of time. However it soon became clear that freedom and choice extended into the funded DB pension world and with it came a host of problems and opportunities for trustees and pension scheme managers.

We are still in the early stages of the experiment; however it is clear that the industry still has many significant processes to change to ensure members retire well informed. For many members, especially those with DB and DC pension funds at retirement, the creation of a retirement plan can be very daunting and quite possibly the most significant financial decision they will make in their lifetime, and with some decisions there is no turning back. More choice usually means more confusion, and with freedom and choice in pensions it also means more risk. The role of the trustees is now vital to ensure members make decisions which are well informed and appropriate to their particular circumstances. For many in DB schemes that will be a conscious decision to stay in the scheme rather than through apathy or a lack of transparency and information.

LV= has been and remains at the forefront of the response to freedom and choice in pensions, and this paper introduces our new thought leadership series that will explore in depth a number of challenges which we believe the industry needs to resolve.

In essence the papers will challenge whether existing retirement processes are still fit for purpose, or whether as an industry we need to explore new ways of communicating with members and implement new processes to ensure we establish a win-win scenario, which means a good outcome for the member and a good outcome for the scheme.

The papers will tackle the arguments around how schemes can ensure that members can achieve good retirement outcomes; how members can be engaged, educated and advised; the increasing requirements for schemes to provide partial transfers; and finally, whether a transfer from a DB scheme should always start with the assumption that it’s not in the best interests of the member.

We will also be discussing these and other current issues at a number of events we are attending and arranging in the coming months, with the content evolving as opinion of leading industry experts informs these papers.

Each week thousands of people in the UK are retiring and need guidance and advice, so this is not a future challenge. It really is time for everyone to wake up to the far-reaching impacts of freedom and choice in pensions.

Steve Lewis,
Head of Distribution, LV= Retirement Solutions
The thought leadership papers in summary

The impact of freedoms on occupational pensions: how to achieve good member outcomes.

This paper has been commissioned by LV= and is written by Billy Burrows, the well-known industry expert on retirement solutions.

In the paper, Billy explores the challenges and opportunities created by freedom and choice in pensions, and how those responsible for pension schemes should respond to help members achieve good retirement outcomes.

- The growth in retirement income solutions available to members and the growing trend to combine different solutions.
- Traditionally, DB and DC schemes have looked to provide members with a guaranteed income. Personal pensions have focused on maximising the pot and converting it into income in different ways.
- DC and DB schemes should embrace the spirit of freedom and choice; a ‘one-size fits all’ approach to retirement income is no longer sufficient, and indeed could arguably increase liability risk for schemes; there is a trend towards more personalised retirement income options.
- Current regulations require schemes to inform members of freedom and choice and signpost them to Pension Wise. Can this really lead to good member outcomes? Can the member be well informed without the knowledge of what the transfer value may be and what the options and risks are if the benefits are transferred to a DC arrangement?

Many in the industry were shocked and did not agree with the significant change in freedom and choice in pensions, however we must acknowledge that the freedoms are upon us now and the benefits belong to the member. George Osborne’s famous budget speech was very clear:

“Let me be clear, no one will have to buy an annuity again… People who have worked hard and saved hard all their lives, and done the right thing, should be trusted with their own finances”

The industry needs to provide the full picture to retiring members, providing transfer values and signposting the options and risks involved in order that they can do the right thing for themselves.

45% of members don’t feel they have the necessary knowledge to make an informed decision about whether or not to transfer.

(LV= State of Retirement report July 2016)
Wake up to freedoms: are current member communications processes working?

This paper will consider the challenges of getting members to take an interest in their options at retirement, and to do this early enough so that a robust plan can be put in place.

Pensions are boring… that’s what we’ve always been led to believe. However since freedom and choice in pensions were introduced there has been a shift in perception especially with DC schemes. Members appear to be taking a lot more interest because they can use the money as they wish. Can DB schemes improve engagement and education to deliver informed decisions?

It is generally accepted that member communications on the whole do not get read until the member is at the point of retirement. Even then they are often too full of jargon and seem to tick regulatory boxes rather than serving members’ interests. Nor do they reduce the risk of members making uninformed decisions.

The paper suggests that the current member communications and engagement processes are inadequate in a post freedom and choice environment. Changes should be made to the annual statement and retirement pack and combined with additional support. The paper challenges the industry to ask if the level of engagement, education and advice provided is sufficient given the significant choices and risks the member is exposed to.

The paper will explore the following questions

- There have been numerous studies which show the level of member knowledge on pension matters is very low. How do schemes increase engagement with their pension provision and the benefits of staying or leaving the scheme? Should transfer values be included on annual statements for all people over the age of 55?
- Engagement is improved when the communications are tailored to the audience. Should statements and other member communications be different for members based on age?
- Should other forms of engagement (webinars, videos, web content, workplace meetings) be used and at what age group should they be targeted?
- To what extent are trustees responsible for member education? Should all members be directed to Pension Wise? And should trustees put processes in place to educate members on their options and the risks?
- If a member wants to explore a transfer how much due diligence and responsibility lies with the trustee to ensure a member is advised by a reputable adviser with advice principles which protect members from risk of ruin?

At LV= we are keen to start this debate. We strongly believe that significant improvements can be made in how members are engaged, educated and advised. We believe the objective is relatively simple; to ensure a member retires making the right choice for them, for the right reasons, with the right support and the right products for their own particular circumstances. The challenge is determining how to achieve this.

Over half of those surveyed have not received information, guidance or advice from their employer, scheme or trustees about accessing their pension under the new freedoms.

(LV= Corporate Solutions DB member research study October 2016).
Wake up to freedoms: should partial transfers be a standard option?

This paper examines the availability of partial transfers from pension schemes, and the impact they have on the scheme itself. We will seek to gain contributions from a number of industry practitioners during the drafting process.

The previous two papers focused on the information and communications presented to members and called for a more tailored and personalised approach. This paper focuses on the ability of the member to personalise the benefits they take from the scheme. Partial transfers would appear to be on the agenda for many schemes however it is still the case that the majority of schemes adopt a ‘one size fits all’ approach of all or nothing.

While it is acknowledged that partial transfers present real challenges in terms of data and administration, many schemes have overcome this. Partial transfers can present a real opportunity for members and the scheme to personalise retirement benefits to the needs of the member.

The paper will consider the following reasons to make partial transfers an option for all DB members:

- It can allow members to achieve flexibility and certainty with their financial plans in a manner which is customised for their own particular circumstances. A partial transfer would allow members to keep a proportion of their benefits so that their essential expenditure is covered and allow them the option to have flexible income through a DC arrangement.

- A partial transfer would enable wealth transfer options to be more flexible. The DC death benefits are extremely flexible with nominee and successor drawdown options. Partial transfers would allow certainty of income and wealth transfer to be achieved.

- Allowing partial transfers can also create a win-win scenario for both the member and the scheme sponsor. EBCs seem to generally agree that there is a saving for the scheme of between 5% and 10% of the deferred value when a transfer is enacted.

- Partial transfers will remove selection bias in the scheme. Allowing partial transfers would ensure a cross section of people transfer benefits rather than a higher proportion of single and ill health members.

Freedom and choice in pensions were created to enable flexibility and choice. Partial transfers from DB schemes enable personalised choice and significantly more flexibility for the member. We acknowledge that for some schemes the technological and administration requirements will need to be overcome, however given that many schemes are allowing partial transfers now this should not be a reason not to allow them.

Subject to scheme definitions, should partial transfers be one of the standard options? We are looking forward to the debate.

Nearly 30% of schemes administered by Lane Clark & Peacock (LCP) include estimated transfer values, and around 15% have decided to offer partial DB transfers.

Source: LCP ‘All change for DB transfers?’ Issue 4, 8 August 2016.
Wake up to freedoms: Should accessing freedom and choice start from a premise that generally transfers are bad for the member and may be harmful to the scheme?

In this paper we turn our attention to: the impact on the scheme of members accessing freedoms; how a good cross section of members accessing freedoms can be achieved, and whether this can be a potential win-win for both scheme and member. As with the paper on partial transfers, we will seek to gain contributions from a number of industry practitioners during the drafting process.

For many years now the perceived wisdom has been that a transfer, or more recently accessing freedom and choice in pensions is not in the best interests of the member and may result in a bad member outcome.

This is evident in the low number of schemes which automatically communicate the transfer value to scheme members, and the number of advisers who have the qualifications and the permissions to conduct safe transfer business. It is even more evident in the significant increase in professional indemnity insurance experienced by advisers who conduct transfer business. Therefore the industry is focused on the transfer of risk from scheme to insurance companies through bulk purchase annuities, buy-ins and buy outs. Freedom and choice have significantly changed this. There are number of reasons why accessing pension savings can be in the best interests of the member and therefore there really is a potential for a win-win scenario provided the scheme achieves a good cross section of members accessing their pension pot.

The paper will explore the following:
- Do we need a change of mindset from trustees? In reality is the fund now equally the member’s money as well as the scheme’s?
- The reasons why accessing pension savings could be in the best interest of a member.
- The inadequate nature and continued reliance on TVAS reports which continue to assume the member will purchase a lifetime annuity after transfer.
- The impact on the scheme if a robust communication process is in place, so that there is a cross section of members accessing their pension savings rather than the fortunate few who historically have had an adviser.
- The safeguards which would need to be in place to ensure a win-win solution.

Freedom and choice in pensions and the change in death benefits now represent a significant change in the role that DB benefits will play for many members reaching retirement. By accessing freedoms the member’s pension benefits could represent a major capital asset which the member could control and use in a flexible manner to match their retirement needs. It can also be used as a family asset to transfer wealth through the generations. A transfer represents a big reduction in uncertainty and liability for the scheme sponsor. Therefore is it time to abandon the premise that accessing freedoms is bad, in favour of a premise that for some members it can be a good outcome and a potential win-win for both member and scheme?

52% of employers say they worry about the impact on the financial mechanics of the remaining scheme from transfers out.

Source: Hymans Robertson research February 2016.
Conclusion

We all know that the retirement landscape has shifted significantly since freedom and choice were introduced.

Occupational pensions are going through a period of transition from an era where the role of the pension scheme was to provide a guaranteed pension for life, be it through a final salary pension or annuity, to an era where the individual wants more control and flexibility over their own retirement income.

The four papers summarised in this document will appear over the coming months and will continue to cement LV’s leading position in the debates regarding retirement solutions, and most importantly in providing the right solutions in this market place.

Look out for the first paper, which will be available in the next few weeks, and do let us know your views on the topics discussed. We are keen that trustees and scheme sponsors keep all that is good about occupational pensions, whilst embracing all that is good about freedoms; choice, flexibility and control.
Contact us

If you want to find out more about LV= Corporate Solutions, please get in touch and we will be happy to discuss your requirements and explore how we can satisfy them.

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