COUNTRY SPOTLIGHT UK

Still shining bright?

With Britain's pension landscape in a state of transition, Talya Misiri **explores how the UK pensions landscape is being overhauled following the gradual shift from DB to DC pensions**

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Britain's pension landscape is in a state of transition. Most visibly in the occupational pensions space, where the scales are tipping from defined benefit to defined contribution pensions. This move has largely been driven by major reforms during the past decade, including pension freedoms and auto-enrolment.

In addition, pensions have been impacted by economic instabilities that have led to traditional final salary pensions becoming unaffordable and less commonly provided among the majority of British employers.

The next phase of the pensions sector, therefore, is set to look increasingly different to what savers have previously been accustomed to. There are evidently lessons to be learnt from soaring DB deficits and schemes falling into the PPF, which have led to the increased uptake of DC savings. With record numbers now in workplace pension arrangements as a result of auto-enrolment, the industry is now looking at encouraging higher contribution levels and more member ownership over pension savings.

In October last year, the Minister for Pensions and Financial Inclusion Guy Opperman's announcement that the Department for Work and Pensions had taken the reins in leading the development of the pensions dashboard project, assured the industry that change is coming.

Lessons learnt

High-profile cases such as the collapse of both high street retail giant BHS and the leading construction player Carillion have brought considerable, negative attention to 'gold-plated' final salary schemes.

There are lessons to be learnt from these cases, Royal London personal finance specialist Helen Morrissey says. She explains that specifically the case of BHS, "gave a powerful warning that employers cannot walk away from their pension responsibilities".

JLT Employee Benefits director Charles Cowling adds that this is a "key lesson" for trustees that "even big, secure companies can fail".

"Close monitoring of employer covenant and contingency planning is therefore vital. Employers must remain conscious that DB pension scheme risks have significant cost and potential impact to the balance sheet and corporate value. Every opportunity should be explored to minimise or remove such risks and their costs," he advises.

It is crucial that trustees understand that scheme sponsors can go bankrupt and therefore, although a scheme may appear to be in a strong funding position on an actuarial basis, this can quickly change. "This illustrates the danger of measuring and managing the scheme's funding level on optimistic assumptions about the future. Hope cannot be a strategy for a DB scheme," Cardano head of innovation Stefan Lundbergh states.

As a result, the Department for Work and Pensions (DWP) confirmed earlier this year that it plans to legislate to make neglect of DB pension responsibilities a criminal offence. In its white paper, *Protecting Defined Benefit Pension Schemes*, the DWP highlighted that it will criminalise company directors and any concerned parties that have wilfully neglected their DB pension responsibilities.

Adding to this, LCP senior partner Bob Scott suggests: "Greater regulatory attention might usefully be paid to those schemes that have

an employer with a covenant that is assessed as being ‘strong’, both to question how robust are the figures behind the assessment and to consider whether it is appropriate for them to run a long-term pensions deficit and/or to take significant investment risk.”

In order to enable The Pensions Regulator to take a more proactive stance in the prevention of pension scheme neglect and reckless behaviour, therefore, it has been awarded greater powers. The white paper confirmed that it will strengthen the regulatory framework and TPR’s powers as set out in the government’s 2017 manifesto.

Evolution

Moreover, it is clear that the UK’s pension landscape is undergoing a significant move from DB to DC pensions. With traditional gold-plated funds no longer affordable for a large proportion of employers, pension saving has switched gears to focus on defined contribution schemes.

The government’s auto-enrolment policy has been instrumental in steering masses of the UK population into workplace pension saving and has resultantly swung the pendulum away from DB to DC.

According to recent data from the DWP, the total amount saved into workplace pensions increased by £4.3 billion to £90.3 billion in 2017. Employers paid in £53.8 billion over the year, while employees contributed £27.5 billion.

AJ Bell senior analyst Tom Selby comments: “The number of people saving in a workplace pension continues to rise as the reforms are rolled out across the country, with matched employer contributions and tax relief increasing the value of member contributions more than three-fold.

“It is also extremely encouraging to see participation levels between men and women are now almost identical.”

In April, auto-enrolled pension savers saw their savings rise to 5 per cent, made up of 3 per cent employee and 2 per cent employer contributions the first of two nudges that will see contributions rise to 8 per cent in 2019, when the employer will contribute 3 per cent and employees 5 per cent.

Nonetheless, the further development the policy, particularly with regards to increasing contribution levels, are needed to provide suitable retirement savings for more of the population.

Aegon head of pensions Kate Smith explains that while increased saving is a positive, greater workplace engagement strategies need to be implemented to encourage members to make higher contributions. Research by Aegon highlighted that just one in five people who are approaching retirement age are saving enough to maintain their lifestyle.

Moreover, the master-trust market is also expected to undergo considerable change with the upcoming master-trust authorisation application period opening in October 2018.

With this, it is expected that a number of these schemes will cease to exist in the market, due to failing authorisation or wanting to leave as a result of increasing costs and tighter regulation.

“This will spell good news for members and prospective employees, as the remaining master-trust providers will be able to achieve the scale that they can then leverage to improve their offering to members,” Willis Towers Watson Lifesight head of proposition development David Bird says.

Innovation

With so much change in the sector, the development of the pensions dashboard has been largely welcomed. Recent figures from Aegon have highlighted that over 700 million people have potentially misplaced some of their retirement savings, with 64 per cent of people with multiple pots losing track of one or all of their pensions. A dashboard that encompasses all of an individuals' pensions data in one place, therefore, seems long overdue.

Additionally, earlier this year, ShareAction found that a "lack of digital innovation and uninspiring saver engagement" efforts by the pensions industry could be jeopardising millennials' willingness to save enough for a decent retirement.

Pensions Management Institute technical consultant Tim Middleton says: "The dashboard will enable members to easily access a wealth of information on their total accrued pension savings. With millennials likely to have around a dozen jobs across the course of their lives, this vital new resource will enable individuals to make more informed decisions about their retirement."

Smith notes: "The launch of a pension dashboard in 2019 should simplify the process of finding lost pensions". She adds: "The hope is that by making all their pensions more visible, people will gradually become more interested in pensions, and in time start to make more active decisions to start to get them ready for retirement."

Nonetheless, the introduction of the dashboard will not automatically drive pensions engagement, Royal London director of policy Steve Webb highlights.

"A pensions dashboard has the potential to boost member engagement with pensions, but only if members can be encouraged to visit the dashboard and to act on

what they see.

"It will be necessary to supplement basic factual information about pension rights with tools which allow individuals to see if they are saving enough for retirement."

While the details of whether employers or providers will be encouraged to provide additional information to employees, if there will be one or multiple platforms and whether schemes will be required to provide member data by law are yet to be confirmed, the Minister has assured of its upcoming introduction to the market.

Speaking at a Work and Pensions Committee meeting late last year, Opperman stated: "We'll see it *[the dashboard]* very soon and before 2020 without any shadow of a doubt".

Less certain, however, is the development and introduction of collective defined contribution schemes into the pensions landscape. Following the closure of Royal Mail's DB scheme and its ambition to introduce a CDC scheme for its members, this scheme type has come back onto the agenda.

Comparing to the UK's European peers, Newton Investment Management head of DC pensions Catherine Doyle states: "Unlike other European countries such as Germany and Holland, the UK does not have a recent tradition of collective savings schemes. CDC would therefore represent a significant restructuring of the UK pensions landscape, which is characterised by its fragmentation, albeit undergoing consolidation."

While there is much debate as to whether the introduction of these schemes are the right step to bridge the gap between employer and employee responsibility over pensions, it could be argued that CDC fits as a halfway point between DB and DC.

Portafina managing director Jamie Smith-Thompson argues: "CDC schemes are like a halfway house that will really appeal to many people. By pooling money together, you haven't got a guaranteed benefit, but instead, you will be better off than on a 'gauge-your-own' investment."

Overall, it's clear that the UK pensions landscape is undergoing considerable change that is likely to shape the sector for years to come. Increased powers for TPR is likely to create a more proactive regulator to prevent downfalls, DC workplace pensions now have record numbers of savers and the impending introduction of the dashboard is likely to overhaul the way in which savers understand and engage with their savings.

When asked what's next on the agenda for the UK pensions sector, ABI director of policy, long-term savings and protection Yvonne Braun exclaims: "Lots of things! Before the summer, we are expecting the FCA's retirement outcomes Review, the pensions dashboard feasibility study, FCA's work on non-workplace pensions, the government's green paper on social care, and further engagement with DWP on their plans to improve the defined benefit sector." ■