Report kindly sponsored by:

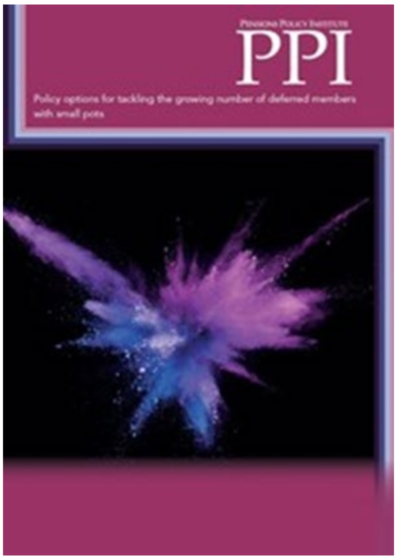
NOW: Pensions

PENSIONS POLICY INSTITUTE

PPI

Policy Options for tackling the growing number of deferred members with small pots

Launch write up:



The Pensions Policy Institute (PPI) held a policy seminar on 23rd July 2020 to launch *Policy Options for tackling the growing number of deferred members with small pots*, sponsored by **Now: Pensions.** This report explores the potential outcomes on the number of deferred pension pots, charges for members and costs for providers of a range of policy options. The event was run as an online seminar with the key findings presented by the author, responses from the sponsor and Stephen Timms, MP, Chair of the Work and Pensions Select Committee, and a wider panel discussion with representatives drawn from regulation, Government, industry and consumer representation.

Just under 100 people representing a broad range of interests within Government, the investment industry, the pensions industry and the third sector attended the seminar.

Maddi Forrester, MFS Investment Management and PPI Council Member chaired the event.

Presentation of key findings and responses to the report

Dr Mark Baker, Senior Policy Researcher, PPI, presented the key findings from the report. The growth of pension participation through automatic enrolment has changed the demographic of pension savers, resulting in many members accruing multiple small pots. The projected proliferation of these small pots has implications for both members and providers. Several policy options, developed through a policy roundtable, were introduced and the impact analysis they could have on the number of pots and the consequential impact upon associated costs and charges incurred. The trade-offs of the policy options were noted including the complexity and potential ramifications of implementation, and how effective they may be considering the degree of coverage they offer, and the reliance upon and encouragement of behaviours and engagement.

Stephen Timms, MP, Chair of the Work and Pensions Select Committee, recognised the challenge of the issue of small pot proliferation and the risk it can pose to the gains made through automatic enrolment. He outlined concerns of the committee and how they intended to address them through a three-part enquiry to be launched at the end of July on the theme of pensions freedoms: five years on. The first part of the enquiry will focus on pension scams. The committee has a specific interest in small pots and is due to imminently publish an open letter to industry (published 31/7) asking for the contribution of ideas and evidence to address the problem of proliferating small pots. Their recommendation is that under the Department for Work and Pensions review of the charge cap and charging structures in 2020 flat fees are not applied to dormant pots alongside other measures. The desirability of consolidating small pots will be considered early next year and they are seeking feasible solutions for consolidating small pots.

Adrian Boulding, Director of Policy, Now: Pensions and PPI Governor, welcomed the action being taken by the Committee and looked forward to suggesting solutions. Automatic enrolment had increased the number of pension savers by reaching out to new groups and demographics. These new savers are largely saving into schemes provided by master trusts. These are generally new schemes set up to address the needs of automatic enrolment. The behaviour of these new savers at retirement would be influenced by the sizes of pots they hold and consequently by any consolidation action. Typically, at retirement savers are only using pots of £30,000 and upwards to provide retirement income, while smaller pots are just cashed in. The benefit of reducing costs through consolidation could benefit the new master trusts and allow them to direct additional spending towards future needs and improve the standards they operate to. Employers who are brought in through legislation (i.e. small employers who introduced a pension offering as a result of automatic enrolment) are doing the statutory minimum and will not be supporting people when they are no longer employed by them. There is no simple solution, but solutions will have to be low cost and work at scale and must be demonstrably good for members.

Panel discussion and Q&A

The following points were raised during the discussion chaired by Maddi Forrester with a panel consisting of Fiona Frobisher, Head of Policy the Pensions Regulator, Rob O'Carroll Automatic Enrolment and Nest Policy, DWP, Alastair Reed, Principal Policy Adviser, Money, Which?. This session was held under the Chatham House rule and the views expressed do not necessarily reflect the views of the Pensions Policy Institute or all panellists.

The following themes of discussion emerged in the panel discussion and Q&A with the audience:

The scope of the problem and potential solutions

There needs to be a view of what a successful resolution looks like to all parties and there needs to be an alignment of interests. This would help to understand what can be achieved without mandation.

The member was considered to be central to how this issue is taken forward. There is an opportunity to look at small schemes which typically contain smaller pots and may not achieve adequate standards. Much information is only gathered at pot level which therefore recognises behaviour may change if pots were consolidated and members took action not on a single pot but on entire pension saving. There is a need through any process to recognise member concerns and implement safeguards, so a consolidator option, for example, may need a Government approval.

There is no simple solution and the trade-offs need to be considered in the round. There must be consensus between all stakeholders to get this done properly.

Sense of urgency

There is a sense of urgency, the longer this goes on the more money savers lose out on. However, there is optimism that action can be taken and progress can be made.

The pensions industry is currently in a data gathering phase, however there are things that can be addressed more immediately, e.g. multiple pots with the same provider.

Care should be taken to avoid an immediate but Pyric victory. It is therefore imperative to not undermine any future action.

Retirement behaviours

Observation of member behaviour indicates they cash in small pots. Master trusts are primarily concerned with accumulation so the issue of decumulation is on the horizon and will need to be addressed.

There is a challenge around the Money Purchase Annual Allowance (MPAA) and its interaction with retirement which is becoming an increasingly complex process with people dipping in and out of employment around retirement in recent years.

Refund of small pots

There was discussion of short service refunds for very small pots for those who just miss their opt-out window. This would have the potential benefit of avoiding a poor member experience and removing a very small pot that is not wanted by either member or provider. There were considerations of whether employer contributions should be refunded however any action would need to be member led.

It was observed that there was no direct awareness of member complaints as a result of this situation and the amount of data upon the subject was limited. To be able to assess the situation more clearly, would require data on the number and scale of such micropots.

There were concerns that this went against the principles of automatic enrolment.

Report kindly sponsored by:

Pot for Life

There was consideration of the implications of operating a pot for life system (as a voluntary selection for a member, potentially with a default option). At the introduction of automatic enrolment this may have been a step too far and would still represent a huge change to a system in its infancy.

Experience from Australia suggests only 30% of members use a default facility and this is driven by marketing from providers wishing to cherry pick desirable members. It was considered there is a significant danger where this process may be driven by provider marketing rather than member interests.

The use of NEST as a consolidator

There was debate about whether NEST could act as a consolidator of small pots. The Government subsidy would mean that the economic desirability of these to a provider is not an issue. However, for Government to progress this would be beyond the scope of NEST as it stands and there would need to be a cost benefit analysis (including to tax-payers) of such an action and consideration of how this interacts with state aid.

A Pensions Policy Institute report

Kindly sponsored by...