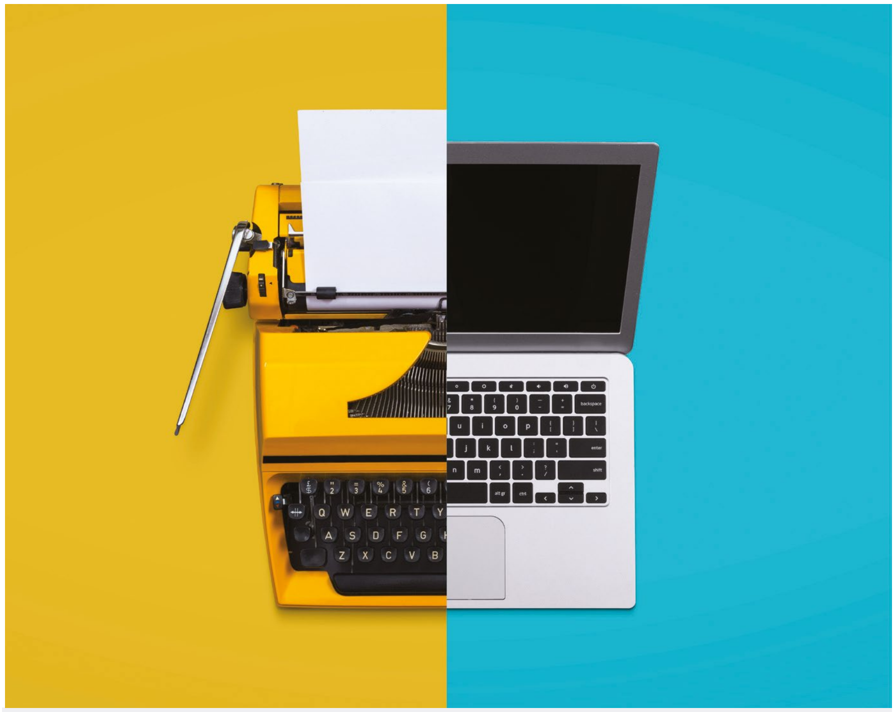

Summary
• As DB schemes continue to be gradually phased out, it is imperative that DC retirement outcomes take centre stage.
• Recent studies have found that providers and regulators are increasing their focus on DC retirement outcomes.
• These efforts are crucial as more members begin to retire with purely DC pensions.
• Initiatives such as pensions dashboards and the value for money framework could help boost member understanding and outcomes.

Out with the old, in with the new

Jack Gray investigates pension providers' and regulators' increased focus on DC retirement outcomes

With DB schemes continuing to be phased out from the UK pensions landscape, pension providers and regulators are increasing their focus on DC retirement outcomes. While most people retiring today will likely be drawing at least part of their retirement income from DB pension, the era of pure DC retirement is fast approaching.

"Fundamentally, DB schemes were intended to provide an adequate retirement income for their members, providing the security of income for life with increases that protect pensions against inflation," says Ross Trustees trustee manager, Annabelle Hardiman.

"As we transitioned out of DB schemes, DC schemes became a means of supplementing this income. Yet as employers have moved towards offering DC schemes only, there has been increasing concern amongst pension professionals as to whether these pots will be sufficient, due to the nature of DC pension provision being heavily dependent on contributions."

Regulators have recognised this, with initiatives such as pensions dashboards and the value for money framework in development, while studies show that pension providers and schemes have been taking steps to prepare for the new world of retirement.

One such study is Aon's *DC Pension Scheme and Financial Wellbeing Survey,* which finds that the proportion of DC schemes that cite 'providing an adequate retirement income' as their main aim has increased from 29 per cent in 2020 to 46 per cent this year.

However, employers may be playing catch up, as the same survey reveals that just 19 per cent of sponsoring employers have considered pension outcomes in relation to their future workforce planning.

Increasing focus

Alongside the move from DB to DC pensions, there are several factors that mean efforts to understand and improve DC retirement incomes have been stepped up. Pensions and Lifetime Savings Association (PLSA) director of policy and advocacy, Nigel Peaple, notes that the population in the UK is ageing, with the number of people of state pension age and older expected to grow by 24 per cent over the next 25 years.

"As the balance of pension provision continues to switch from DB to DC, these future retirees will have increasingly large DC pots to manage, while numbers retiring with a guaranteed income will decline," he adds.

Furthermore, the introduction of

pension freedoms in 2015 means that it is more important for those retiring with DC benefits to have a better understanding of their pension savings and finance in general than those retiring with DB benefits. This is also a factor in providers and schemes increasing their focus on retirement outcomes as they aim to provide DC scheme members with better support as they approach retirement.

Peaple continues: "Pension freedoms, having given people new possibilities to choose how to draw their DC pension savings, also mean people need more help to make the best choices for their circumstances.

"Our research has shown that workplace pension schemes want to be a major part of the solution in creating a bridge between a system that uses the power of inertia to successfully bring people into pension saving, and the decisions they must take to access their pension saving in retirement.

"These decisions are complex; not only will these retirees be taking the investment and longevity risk, but their needs will likely change from the point of retirement – when they may like more flexibility – to later on when a steady, sustainable income may be more suitable. This makes designing retirement income products an important priority for pension schemes today."

Finding a solution

With the scale of the challenge of achieving good DC retirement outcomes becoming ever-more apparent, the industry, regulators and the government have been attempting to find solutions to help members and schemes with the changing landscape.

The Financial Conduct Authority's (FCA) Investment Pathways is one such initiative, whereby drawdown customers can select pre-prepared 'pathways' that define how they access their retirement income. "Investment Pathways are a step in the right direction, helping to alleviate anxieties and delivering on the promise to firm up retirement options, in particular for non-advised savers who are yet to draw down," says Legal & General Investment Management (LGIM) co-head of DC, Rita Butler-Jones.

"Those who previously confessed to having their head in the sand told us that this was a positive first step, a relatable and simple way to make retirement choices feel tangible, with a focus on the outcome of each decision."

Additionally, the FCA and The Pensions Regulator (TPR) are developing a framework for developing value for money in DC pension schemes, which has been proposed to be made up of three 'key elements': Investment performance; scheme oversight, including data quality and communications; and costs and charges.

"The more stringent value for member requirements coming into effect from this year will put a spotlight on what 'good' means for DC pensions savers, with charges and member communications being key factors for trustees to consider," comments Hardiman. "The launch of the pensions dashboard will also give savers greater visibility of their savings as a whole, and more meaningful data to measure retirement outcomes with."

However, Natixis IM head of DC strategy, Nick Groom, is less confident with the regulators' value for money proposals: "The industry needs to now focus on quality retirement outcomes. For employees, workplace pensions have become the only vehicle in town.

"However, unfortunately, amongst other dynamics, the market decided that cost was a function of value for member. This has created an unwanted competitive playing field where life companies in particular have driven fees down in a race to the bottom to extraordinarily low levels to capture new business. This has pushed the quality of investment design and options included in these schemes down to worrying levels."

Groom states that the "one lever we have left" to help build better outcomes for DC savers is the investment quality of default funds.

"This is all happening whilst the government is now trying to convince the DC market to include private assets, like venture capital funds that come with a fee level of 200bps, and performance fees on top, having regulated in a fee cap in the first place," he notes.

"Of course, the drive for consolidation will help to create appropriate scale, and that scale gives the buying power to create a more sophisticated and diversified investment process."

Moving forward

As the pure DC retirement world gets nearer, industry figures believe that the focus on outcomes will only increase. "As more people with purely DC pension pots begin to retire, I expect that adequate retirement outcomes will be increasingly considered when setting out new pension regulation," says Hardiman. "For those retiring over the next 10 years, this may be too little too late, but some solace can be found from the lessons the industry has learned."

Butler-Jones adds: "For future retirees, it's likely that their DC pot will be their only source of retirement income. As drawdown continues to become a more popular choice for savers, the need for better support will continue to grow."

To better support savers, the PLSA has called for a new set of product, communication and governance standards. Peaple explains: "Our proposals – called Guided Retirement Income Choices – are designed to complement pension freedoms and build on existing governance, regulatory approaches and guidance services, to provide member support throughout the retirement journey and develop product mixes that cater for the evolving needs of retirees over the course of retirement."

Written by Jack Gray