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Department for Work and Pensions
Caxton House
Tothill St
London SW1H 9NA

24 January 2024

Dear Sir or Madam,

We are writing in response to the Department's call for evidence on introducing a 'lifetime provider' model into the private pensions market, whereby an individual saver could choose their own pension provider and this would then 'follow' them for the rest of their career (with the ability to change provider at any time).

Automatic enrolment has been one of the great policy success stories of modern times, helping 11 million employees save into a pension. While there are gaps in provision, this is a fantastic achievement of which the Department and successive Governments should be proud.

However, we are concerned that introducing a lifetime provider model, in effect switching the defined contribution system to a retail marketplace, would be highly disruptive and lead to poor outcomes for mass market savers.

Additional costs for most savers

While it may be a laudable long-term aim, there is a substantial risk that it could lead to the highest earning employees simply opting out of their employer's arrangement and finding a better deal elsewhere, leaving the majority of employees left in its default fund. This is driven by a general lack of engagement – the FCA found only 25% of savers are 'very engaged' with their pension, and there is no evidence to suggest that even this group would take good decisions.

This would lead to the removal of any cross-subsidy, whereby more profitable savers would no longer be helping keep costs down for lower-income (and less profitable) savers, potentially leading to higher charges for those remaining in default arrangements. We are concerned this could undermine DC providers' business models and lead to higher charges, as could the increased marketing costs that are likely to be experienced as a result of switching to a retail market.

Higher charges make a significant difference to a saver's retirement income. DWP modelling conducted ahead of the introduction of the charge cap in 2014 found that increasing the annual management charge from 0.5% to 1%[i] can make a difference of about £1,000 income a year – a huge amount to someone on a low income (this would

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likely be even more today, as annuity rates are higher). We are therefore concerned that higher charges would be hugely damaging to future generations of retirees.

Sequencing

We are supportive of the Department's efforts to implement the proposed Value for Money (VFM) framework. We believe this would be an essential pre-requisite for moving to a lifetime provider model. However, this is currently aimed at industry and professionals, whereas a consumer-facing VFM framework would be required. Currently, there is no consistent, independent and reliable information available that would allow savers to compare schemes.

We believe that improving income adequacy in retirement is the main goal of pension saving. The current contribution rates are generally regarded as insufficient, and we support wider proposals to increase this, especially by raising employer contributions. However we believe that this debate needs to be settled prior to any fundamental changes to the marketplace. We encourage to prioritise this future vision of pensions, rather than pursuing a lifetime provider model at the present time.

We also believe that several new consumer protections would need to be in place in order to make this a success. This includes a new regulatory environment with consistency across all schemes and significant investment in enforcement; meaningful protections against scams, including a right for employers to refuse to make payments into a scheme where they believe it is fraudulent; a reduced charge cap set at a maximum of 0.5%; a banning of 'introductory offers'; and sophisticated information and advice available to help *all* consumers make the best choice possible.

Behavioural bias

We know from auto-enrolment that inertia is very powerful, and is the main driver of the increased numbers of people saving. This stretches even beyond pensions, for example, in the Nest Sidecar Savings trials, only 1% of people proactively chose to save, compared to 46% who said they would like to. Even in Australia, a DC pensions market that has matured with the lifetime provider model built in, it is estimated that only 7% of people actually switch out of their default provider. Giving people the ability to switch schemes also significantly increases the risk of people opting out.

This could be exacerbated when people learn that their pension is invested. This is distrusted by many – polling has shown that two thirds of people are nervous about putting their money in risky assets.[ii] Furthermore, research by Hargreaves Lansdown found that only 35% know their pension is invested[iii] - this widespread aversion to loss could put many, especially those on lower incomes and women (who are known to be less trusting of investments), off saving for their retirement.

We trust that the Department will take an objective view in reviewing all the evidence, fully considering all the downside risks as well as any possible benefits. We look forward to hearing the outcome in due course.

Yours faithfully,

Christopher Brooks
Head of Policy, Age UK

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[i] Charges in Qualifying Pension Schemes, Impact Assessment (2014), Department for Work and Pensions
[ii] https://www.wealthify.com/blog/fear-of-investing-dispelling-investment-myths-as-new-research-shows-66-of-brits-are-nervous-about-investing
[iii] https://www.pensionsage.com/pa/One-third-of-savers-unsure-if-their-pension-is-invested.php