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GENERAL COMMITTEES

Public Bill Committee

PENSION SCHEMES BILL

Third Sitting

Thursday 23 October 2014

(Morning)

CONTENTS

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Monday 27 October 2014

STRICT ADHERENCE TO THIS ARRANGEMENT WILL GREATLY FACILITATE THE PROMPT PUBLICATION OF THE BOUND VOLUMES OF PROCEEDINGS IN GENERAL COMMITTEES

The Committee consisted of the following Members:

Chairs: Mr Peter Bone, †Mrs Linda Riordan

Abrahams, Debbie *(Oldham East and Saddleworth)* (Lab)
† Blenkinsop, Tom *(Middlesbrough South and East Cleveland)* (Lab)
† Coffey, Dr Thérèse *(Suffolk Coastal)* (Con)
† Graham, Richard *(Gloucester)* (Con)
† Hammond, Stephen *(Wimbledon)* (Con)
Hemming, John *(Birmingham, Yardley)* (LD)
Kwarteng, Kwasi *(Spelthorne)* (Con)
† Latham, Pauline *(Mid Derbyshire)* (Con)
Love, Mr Andrew *(Edmonton)* (Lab/Co-op)
McCann, Mr Michael *(East Kilbride, Strathaven and Lesmahagow)* (Lab)
† McClymont, Gregg *(Cumbernauld, Kilsyth and Kirkintilloch East)* (Lab)
McFadden, Mr Pat *(Wolverhampton South East)* (Lab)
† Maynard, Paul *(Blackpool North and Cleveleys)* (Con)
† Mills, Nigel *(Amber Valley)* (Con)
Morris, James *(Halesowen and Rowley Regis)* (Con)
Paisley, Ian *(North Antrim)* (DUP)
† Watkinson, Dame Angela *(Hornchurch and Upminster)* (Con)
Watts, Mr Dave *(St Helens North)* (Lab)
† Webb, Steve *(Minister for Pensions)*

Matthew Hamlyn, *Committee Clerk*

† attended the Committee

Witnesses

Dominic Lindley, consultant

Matthew Oakley, Head of Economic Analysis, Which?

Tim Sharp, Pensions Policy Officer, Trades Union Congress

Chris Curry, Director, Pensions Policy Institute

Dr Ros Altmann, pensions expert

Jane Vass, Head of Public Policy, Age UK

Public Bill Committee

Thursday 23 October 2014

(Morning)

[Mrs Linda Riordan *in the Chair*]

Pension Schemes Bill

11.30 am

The Chair: May I remind hon. Members that mobile phones should be switched to silent and that tea, coffee and any refreshment other than water are not allowed in Committee?

Examination of Witnesses

Dominic Lindley, Matthew Oakley and Tim Sharp gave evidence.

11.31 am

The Chair: I have spoken to the Minister and shadow Minister and they have agreed that we do not need to go into private session to discuss questions before we hear from the witnesses today. We will hear oral evidence from Dominic Lindley, consultant, Matthew Oakley, head of economic analysis, Which? and Tim Sharp, pensions policy officer, Trades Union Congress. For this session we have until 12.15 pm. Would the witnesses please introduce themselves for the record?

Matthew Oakley: Good morning, I am Matthew Oakley, head of economic analysis at Which?

Tim Sharp: I am Tim Sharp. I am policy officer at the Trades Union Congress focusing on pensions and investments.

Dominic Lindley: Good morning, I am Dominic Lindley, an independent consultant on consumer and pensions issues.

The Chair: Thank you. I will now call Members to ask questions.

Q165 Stephen Hammond (Wimbledon) (Con): May I start by asking Mr Oakley to give the view of Which? on what the guidance guarantee will deliver? Which issues still need to be rectified?

Matthew Oakley: Obviously, there is some uncertainty about how it will work in practice. We want to see a three-stage process where you work out how the consumer can get the information they need before the guidance session, ensuring that at the guidance session all the relevant areas of finance are covered so that the consumer leaves that session with an idea of where to take the next steps, to go to an independent financial adviser or to explore a different part of the market.

I guess the concern, particularly with reference to the Bill, is that there will be a proliferation of different types of pension and different types of schemes which might make decisions more complicated for consumers. It is really important that those be explained clearly and that the guidance cover all of those in one pot. Moving on from there, we would like to see a clear evaluation strategy. I have heard a lot of talk about evaluating the take-up of the guidance guarantee, but I think it needs to go much further than that and evaluate each of the three stages that I outlined: take-up; customer experience of the guarantee itself; and then where people are going afterwards. So, are they taking advice from an IFA, are they just sticking with their pension provider or are they going to another place? It is essential to put that in place quite quickly.

Q166 Stephen Hammond: Mr Lindley, what do you think is the level of take-up for collective defined contribution schemes?

Dominic Lindley: They definitely offer potential advantage to consumers. If you explain a defined contribution scheme to consumers they regard it as chaotic. They regard it as investment which they see as like gambling. The more you explain it, the more uncertain they become. The No. 1 question that consumers have when then are enrolled in a pension scheme is, "Can you give me any certainty about what I might get at the end?" When they find out that you cannot give them any certainty they become disengaged. Collective defined contribution schemes undoubtedly have the potential to deliver more certain pensions but also to take away some of the complexity of decision making from consumers. The Bill is about giving people more freedom and that is very welcome, but we also need to recognise that there are some people who do not want to or cannot exercise that freedom. They want the kind of relationship that might exist between a doctor and a patient. They want the kind of relationship that might exist between a doctor and a patient. They want someone to act in their best interests and help them get the best possible pension.

In terms of take-up, one challenge will be to get these schemes to achieve significant scale. Where is the capital going to come from to back them? You need either big employer groups or the National Employment Savings Trust to be interested and offer these schemes, or you need some existing large defined-contribution schemes to want to convert to CDC. That is where the biggest uncertainty is. I absolutely support making them legal, but there is gong to have to be a very detailed strategy for getting the schemes off the ground and helping them achieve scale.

Q167 Stephen Hammond: You are suggesting that there is no evidence of any appetite for it at the moment.

Dominic Lindley: Not among the employers that I know. I think these schemes will develop. The key will be persuading employers to take them up. If NEST were to offer one of these schemes, that could give the market a big boost, as we have seen with NEST changing the market and how schemes are sold to employers.

Tim Sharp: Can I come in on that? Allowing CDC should be seen simply as the first stage. I am not sure at this point that you would expect to see crowds in Parliament square demanding access to Dutch-style collective risk-sharing pension schemes. However, if you asked people, there might be more demand for more secure, predictable retirement incomes. Likewise, employers might not know the nuances of CDC but might be quite keen to provide schemes that would give better outcomes for the same contributions. We hope that bringing in a law is just the first part of this. We are keen to see the Government in particular work on consensus building in developing how these schemes can work in practice, and help build demand.

Q168 Nigel Mills (Amber Valley) (Con): Mr Sharp, following on from that, one way the Dutch have made these schemes successful is that trade unions sponsor them and encourage their members into them in each industry sector. Can you see any prospect of that in the UK? It looks a little unlikely at this stage to me.

Tim Sharp: There is certainly a role for trade unions in working with employers to develop the best pension schemes they can for workers. At the moment, maybe conversations concentrate on contributions. Hopefully, in future they will also look at the types of schemes available. We would expect unions, where they have good relationships with employers, to be working with them, where there are single employers or in helping to develop multi-employer schemes. That is how we would see the role of the union.

Q169 Nigel Mills: You cannot see a car industry workers' collective pension scheme above and beyond individual employers' pension schemes. That is not something that you can see a trend towards.

Tim Sharp: I could see a trend towards industry-wide schemes, and I could see why trade unions might be supportive of those. That is where I would see the trade union role, not necessarily as a provider, though some might want to be more active in that way.

Q170 Nigel Mills: Okay, thank you. Can I turn back to the guidance guarantee? Mr Oakley, you gave us some thoughts about how that might work. I suppose the tension is, where does guidance become advice and how much guidance can you give before you are drifting into regulated advice, which starts to get expensive and risky for the person providing it? What can be done with guidance without crossing that line?

Matthew Oakley: Reading through the responses in the past couple of days, the consensus view has been that that is possible. We are clear that there is a good level of personalised and tailored guidance that can be given helpfully. The key thing is to explain to the consumer what it is they are getting. Even the name—the guidance guarantee—can be quite confusing to consumers. They might think it is guaranteeing them an outcome. They might wonder what the guarantee is that they are getting.

We are keen that the Government, the Financial Conduct Authority and others work with industry to show consumers what they can get and what they should expect. They should know that it is not a distinct piece of advice that says, "You should go and do this." It is saying, "Here is the kind of thing that you can be doing. Here are the questions that you could take away and speak to an IFA about. Here are the questions you should be asking of the products that you are looking to engage with." It would really equip consumers with the tools they need to take the next step, rather than necessarily give them an answer. That is where the difference would lie.

Q171 Nigel Mills: How long do you envisage a guidance session needs to be? Are we talking about a quarter of an hour, half an hour or an hour?

Matthew Oakley: It is going to vary an awful lot, of course. What we are keen on is that it really is a personalised and tailored experience. Some people will have a good idea of what their pension pots and their other investments look like, and they can go into a guidance session and have a clear conversation, and just be signposted to other places. That might be quite a short conversation.

For others, of course, we think that they will need a lot more information and a lot more guidance. That might include a repeat session, or having to come back with more information because they have not come to that first session with enough information. That is one of the key things here: we are worried that not enough is being done, particularly before the roll-out of the guidance guarantee in April, to ensure that consumers know what they need to take to that first session. What we would like to see is a much more concerted effort to ensure that consumers get a full picture of each of their pension pots, alongside each of their other investments, that they can take to that session and really start off on the best possible route.

Q172 Nigel Mills: I suppose the key to making guidance work is that it needs to stick in your head and make you change your actions after you have received it. Do you have any ideas about how we could get the guidance followed up, or checked up on? Perhaps when someone goes to buy a product, say, should there be a kind of follow-up prompt in that situation, saying, "Before you sign on this dotted line, have you had your guidance? Have you thought about your spouse?"? Is that something we ought to be regulating for as well?

Matthew Oakley: This is a discussion around the kind of back-stop option. There are obviously a range of things that you could do here. Obviously there is a worry that people have not had the guidance and that they are then making decisions based on a lack of information, or just not making a decision.

Obviously, regulation is one way of addressing that, with the examples that you put forward. I worry, however, that that could have unintended consequences. So, you could ask, for instance, "Have you thought about whether you have provided income for your partner?" Of course, that pushes someone in a certain way, because we know what people feel emotionally, and so that in itself is not even an objective and clear piece of information for a consumer.

What I think we would like to see, certainly first off, is that pension providers and broader providers are working in the best interests of consumers. That means that they should be working as an industry to get best practice principles about how they deal with this situation, because they know it is coming. We know that take-up estimates vary from 3% to 93%; I imagine that it will be somewhere between those two figures. We know that a lot of people will not take the guidance, certainly initially, so the industry needs to work out how it will deal with that, and it needs to be conscious that we must improve the situation so that people are signposted regularly to the guidance.

Q173 Nigel Mills: So the view of Which? is that we should rely on best practice and not on regulation?

Matthew Oakley: No. I think that is the initial point, and I am thinking back to my point earlier about making sure that we evaluate the system properly. If it is found that people are not taking up the guidance, or that if they are taking up the guidance they are not going to see an IFA or taking other options that are available in the market, then we need to think much more carefully about whether we should and could regulate to ensure that those sorts of options are taken. What I am saying is that we should not necessarily jump to regulation, which can be quite prescriptive and can lead to unintended consequences.

Q174 Richard Graham (Gloucester) (Con): I am a little bit frustrated, because this is your chance to shape the Bill—we want to hear your ideas—and it is all a bit vague and woolly at the moment. Matthew, if I wanted to know what sort of questions I should ask a second-hand car salesman about a car, Which? would give me a checklist of questions I should ask. You are the interim head of personal finance. What sort of questions do you think people should be asked during this guidance? Will Which? produce a report on that? You have done a report outlining areas where Government must focus to boost growth in the long term; how about a report outlining areas where Government guidance on pensions must focus?

Matthew Oakley: That is a very good challenge. I think I will go back to my point that I would not want to prescribe a set of things that must be ticked off and asked of a person in guidance. The key thing here is that it is a personalised experience, and that the people giving that advice are qualified and professional enough to see the whole picture of someone coming in to them and give them a routeway into further options to consider what they need to do.

Q175 Richard Graham: I don't think we are asking you to prescribe, but we are trying to get your best ideas, and I have not really heard one yet. Have a go at thinking about that, because we want to get the maximum out of these sittings.

Matthew Oakley: I go back to my point about making sure that people are coming with the right information. One thing that you could do quite straightforwardly is ensure that there is a one-page summary of each of the pension pots that someone has, which people are provided with before they go to the guidance, which they can collate and take in. That is one distinct thing that could happen straight away. There are various names for this—pensions passport being one of them—and that is an immediate thing that could happen.

In the longer term, you can start to think about whether, as they have done in Sweden with the orange envelope, you could start to have a data-led solution—a midata example, where you have an online platform potentially, where you can bring together information about everyone's pensions pots in one place, alongside the state pension and alongside an understanding of their savings portfolio to really give them that information, so you can start to have discussions with them an awful lot earlier. That is the kind of thing—consumer information power—that we want to see much more of.

Q176 Richard Graham: Tim, what about you? You are the pensions policy officer. I am not quite clear what your policy response to the Bill is and whether you are broadly supportive or have concerns about bits of it. You intimated in your answer to Nigel that trade unions would not really be leading on creating a CDC yourselves, but that you might be working alongside an employer to do so. Has the TUC had those sorts of conversations with large employers that have, for example, existing defined-benefit schemes but might be looking to change them? Try and give us a practical sense of where the TUC is coming from and what it would like to see happen.

Tim Sharp: We are very supportive of measures to bring in CDC. In terms of the law as it stands, these are still the very early stages, in the sense that we still need to flesh out what kind of schemes will be permitted exactly.

Q177 Richard Graham: What would you like to see permitted?

Tim Sharp: We would like to see the broadest possible range. I think that what we really need is a period of discussions between Government and employers and providers, and trade unions and employers, to develop where these schemes should work. So I think there is going to be a very different model in a multi-employer setting than there might be if there is an individual employer interested in improving their DC schemes. The role of the TUC in that is in supporting discussions.

Q178 Richard Graham: You have not had those discussions yet with employers.

Tim Sharp: No.

Richard Graham: But you will be doing so.

Tim Sharp: It is possible. I think it is more likely that affiliated unions would have those relationships with individual companies, but we are very happy to talk to anybody who wants to discuss the merits of CDC pensions.

Q179 Richard Graham: Dominic, you are a consultant; does that mean that you have clients with pension schemes and that you have been talking to them? I thought you were quite vague, again, in your answers to Nigel. What is the level of interest that you are seeing either in defined-ambition or the collective DC options that the Bill provides for? Are you saying that they are of some interest?

Dominic Lindley: They are of interest, but of limited interest so far. One of the big concerns is where the capital is going to come from to establish these schemes, because you either need to charge the new members at the start a bit more to build up that smoothing fund, or the capital needs to be provided by an existing insurance company or other provider.

In terms of the guidance guarantee, I am also a trustee of a pension scheme with £100 million-worth of assets, so this is certainly an area where the retirement income market—the inertia and complexity—has delivered really poor outcomes for consumers for many years. The guidance guarantee is absolutely welcome, but unless we take further action and introduce extra lines of defence, you are still going to get insurance companies defaulting people into very poor value products. They have been defaulting people into poor value annuities for years.

Q180 Richard Graham: So what will your scheme do to prevent that?

Dominic Lindley: First, there will be strong governance around the options offered, and because it is a trust-based scheme, there will be a strong duty for me, as a trustee, to act in the best interests of my members when selecting the products, whereas that is completely absent for insurance companies.

One of the things you could do is this. New clause 5 gives the Department the power to impose a duty

"to act in the best interests of members".

At the moment, the intention is that that will apply only to the CDCs, whereas you could expand that power to give insurance companies a duty to act in the best interests of members. That certainly would preclude them from offering annuity rates 20% off the market best. If my mum takes out an annuity with a rate 20% off the market best, that is like taking the last 11 years of her pension contributions out into the street and just burning them. Nothing in the Bill introduces that strong governance around retirement income processes.

However, there are also some extra lines of defence that need to be introduced. You could expand the charge cap, which at the moment applies only during the investment phase, to income draw-down arrangements. You could require, as was suggested earlier, an extra line of defence by getting pension schemes and providers to ask specific questions at the point at which people are making decisions.

Q181 Richard Graham: Do you have an idea of what specific questions those would be?

Dominic Lindley: First, regarding tax arrangements, there is a big risk if you draw down your pension over one tax year that that could push you into the higher rate tax band, so people need to be clear on that. They also need to be clear on what they will live on if the money runs out, the financial position of their partner, their entitlement to state benefits and whether they have any health conditions.

However, there is also a fundamental issue with the definition of pensions guidance in the Bill. At the moment, pensions guidance is defined only as helping you to decide what to do with your pension, whereas we know that for many people the defined-contribution pension is only a small proportion of their household wealth. For one family in four, the defined-contribution pension represents only 4% of their total financial wealth.

If I was sending my mum to get guidance about how to maximise her retirement income, I would want the person to ask questions about her existing assets, her savings, how to get the best deal on them, where the investments were and whether she was claiming all the state benefits to which she was entitled. At the moment, the definition of guidance in the Bill kind of precludes that. You hope that people such as the Pensions Advisory Service and Citizens Advice would cover those issues in the guidance, but at the moment that is not in the Bill.

Finally, we need everyone to review the default investment option in their schemes. In most pension schemes, the default investment option is targeted towards people buying an annuity at age 65, whereas we know that that is not going to happen for many people in the future. But if your default investment option is, say, to go into cash at age 65 and then the consumer is just leaving it in the pension scheme for 20 or 25 years and not actually drawing much of an income out of it, you will not only be losing money in real terms, but losing money in nominal terms. Some of the cash funds offered by pension providers are actually losing consumers money, because their charges are greater than the tiny rate of return you are getting on cash at the moment.

Again, at the moment, in a trust-based scheme, there are strong duties on the trustees to act in the best interests of members. Those duties are absent for insurance companies and for contract-based schemes. We are kind of relying on the FCA, and as you saw earlier in the week, the FCA does not seem to want to introduce even the second line of defence by getting providers to ask specific questions at the point at which people access their pension.

Richard Graham: Thank you; that is very helpful.

Q182 Dame Angela Watkinson (Hornchurch and Upminster) (Con): One of the most important things to a pension saver is certainty about what will happen at the end of their working life when they retire, so that they can plan their retirement and have some certainty about their retirement income. Do you think that the new shared-risk schemes will increase certainty, compared with existing defined-contribution schemes?

Tim Sharp: On collective defined contribution, where we have the greatest hopes, the modelling that we have seen certainly shows more stable increases in the size of the pension pot and greater increases, so we would be hopeful that that would meet that sort of demand.

Q183 Dame Angela Watkinson: Do you think that the increased complexity in the range of pension schemes available to people now will result in higher take-up than we see at the moment?

Tim Sharp: There is clearly a need to build trust in the pensions system. Dominic touched on this as one of the issues. One of the slight concerns we have about the Bill is about governance. That has been tightened up, but we think that it is important that consumers have trust, particularly in new forms of pension scheme, so we would regard, for instance, CDC as being most appropriately introduced under a trust-based model, whereby trustees are obliged to act in the interests of scheme members. I am talking about those sorts of development. A general move in the market towards trust-based schemes would help to foster trust and over the longer term build contributions and participation in pension saving.

Q184 Dame Angela Watkinson: Do you think any further regulation is needed to increase that and could it be included in this Bill?

Tim Sharp: We are disappointed that when it comes to the new forms of pension scheme, contract-based arrangements can be allowed. We think there are too many conflicts of interest when a provider must not just think about acting in the interests of scheme members but also has that profit motive. We think that schemes are best as not-for-profit trusts that then contract in services from elsewhere. We would prefer to see things like CDC only introduced under a trust model.

Q185 Dame Angela Watkinson: Do you see any difficulty in the new shared-risk schemes having a viability level, and that people will want to hold back and see how successful they are before they join them? If they do not join them, they will not reach that volume whereby they can achieve viability.

Tim Sharp: The hope would be that employers with large schemes would initially convert to one of these new models such as CDC, therefore providing some initial capital. You can easily envisage two or three big employers, which already take their pension provision very seriously but currently have DC schemes, looking to move to things like CDC. The challenge will be rolling that out across the market and seeing the development of multi-employer schemes and so on. We think there could be a role there for allowing NEST to operate a CDC scheme as a way of building scale in the market and showing that it is viable.

Q186 Gregg McClymont (Cumbernauld, Kilsyth and Kirkintilloch East) (Lab): Dominic, you gave a useful and detailed list of things, taking up Richard's challenge to fill in many of the blanks in the existing guidance proposals. Have any of your organisations been asked to contribute to the Treasury's development of the guidance guarantee?

Dominic Lindley: I have not personally.

Q187 Gregg McClymont: So we are all working with a foggy mist descending on this policy area. On the question of making this guidance guarantee worth the paper it is written on, first and fundamentally, how can you help individuals to predict their own longevity?

Dominic Lindley: I don't think you can. People underestimate their own longevity. What you need to do in terms of withdrawing from your pension is to be clear at the start and it needs to be reviewed regularly. Not only do you need a pensions passport at the start—because if you have four separate pension schemes you need to bring them together, know where they are invested and know how much you have in total—but you almost need some kind of dashboard which, as you withdraw money from your pension every month, shows you whether you are going too fast or too slowly. That is the other risk: you just leave the money accumulating and do not spend it, even though you need it. If you are given a pensions dashboard, which shows at your current withdrawal rate when you will run out of money, then you can adjust that.

One of the big issues about income draw-down is that more people will use it and those products have both investment and longevity risk. If you live through a period of very volatile returns, like the financial crisis, then if you keep withdrawing at the same rate you will pretty soon run out of money. So the guidance guarantee not only has to be an at-retirement thing; it has to have space for regular review. Fundamentally, on income draw-down, those products have to offer value. You are taking extra risk by staying invested in riskier assets. If all of that extra return is going in charges, you are not getting any benefit.

Finally, annuities are not going to completely disappear. Many of them will be bought later and will remain appropriate for people to buy at much later ages. We have to make sure that people get asked proper questions about medical history. We have to stop insurance companies offering poor rates. So you can put regulation on insurance companies to act in best interest or you can set up an annuity clearing house like they have in Chile. If a consumer wants an annuity quote, they can go to the clearing house and get a competitive quote even though that might not be the absolute best.

Q188 Gregg McClymont: Thank you for that very useful answer. Does the panel agree that we are clearly moving towards a system of much greater participation in draw-down? While the phase of building up the pension has been a thrust towards better, not necessarily more, regulation with better quality criteria and the like, as we move into the new draw-down world there is none of that as things stand. There is no proposal from Government to extend the cap, as you suggested, into the draw-down phase or to have those quality criteria that are there in the building of the pension pot. Is that surprising? Is it a problem? Have you heard anything about the possibility of the Government moving?

Dominic Lindley: Not at this stage, but I think we are all relying a bit too much on the FCA to act on those things. As we have shown, with its proposals on independent governance committees, it is not imposing the kind of governance arrangements and duty to act in the best interests of consumers that most consumers need. If the FCA is not willing or able to do it, that is where the Government are going to have to step in.

At the moment, the FCA seems focused on setting standards for the guidance guarantee, which are very important. It is almost designing a leaflet to ensure take-up when it should be focusing a lot more on the regulation of insurance companies and the emergence of some alternative products. You probably will not have people being sold annuities any more. They will be sold secure income plans, which will be fixed-term annuities for a number of years and then you will get your money back. The FCA should be watching closely and reviewing every single product when it comes on to the market.

The final thing, and one that worries me, is people falling prey to scams early next year. If you search for pensions advice or guidance on Google, you will get a lot of websites where they are not actually providing you with pensions advice or guidance. All they are doing is getting you to type in your information, which is then sold on to various people. We must have additional warnings for people who fall prey to unregulated investments and scams.

Even if you go into a high street bank, if a very elderly person comes in and withdraws large amounts of cash, most staff would have been trained to ask questions about that and double-check. Those sort of policies are completely absent with insurance companies. They have never really had to think about them before. They need to do some thinking pretty quickly before next April.

Q189 Gregg McClymont: I intend to move on to CDC shortly. First, the FCA's evidence seemed extraordinary to me, making it clear that it would not get involved in anything other than setting the guarantee guidelines, and would not get involved in those extra lines of defence. Have you any opinion why that might be? Is it a capacity or philosophy issue? We know that the FCA does not have a great record on pensions.

Dominic Lindley: It is partly philosophy. The FCA is very driven now by risk it identifies. It has a kind of conduct risk outlook that identifies the risk across lots of different financial products. There is virtually nothing about auto-enrolment pensions or workplace pensions in the previous conduct risk outlook. It has been doing a market study on annuities for about nine or 12 months. Even when that market study concludes, it will then go into a next stage of proposing changes, which will probably be too late. There definitely needs to be a greater sense of urgency.

Tim Sharp: We're concerned that the guidance guarantee maybe gives a false sense of security that somehow, through a half-hour session, you will create this perfect consumer operating in a perfect market. A lot of Government policy so far, through auto-enrolment or the charge cap, has accepted that it isn't there and is very hard to create. We think there should be a lot more emphasis on helping schemes to develop strong default options. Particularly with the time scale of bringing in the freedom of choice measures, the schemes are reporting that they are not necessarily going to be able to do all that they would want to bring in robust retirement income options for scheme members. That concerns us greatly.

Matthew Oakley: I share that concern, particularly around whether we are going to see a continued inertia from consumers. Again, I go back to the point that we really need to keep testing this and have a clear evaluation strategy that says who is taking the guidance, what they are going to do with it, and who has continued to stay with their pension provider when they hit retirement and what are they going into. If we decide in six months, or a year or two, that we have not had an improvement in this market in terms of consumer engagement and making informed choices, we need to consider much broader options. There are other options out there: there is potential for a state-backed scheme, post-retirement; there is potential to draw on the example of NEST, and to use a default scheme on the decumulation side as well. There are options there that we can take, but I would not rush into them right now.

Q190 Gregg McClymont: Matthew, perhaps I am putting you on the spot, but do you think that the Financial Conduct Authority's history in this area suggests that it is up to that task?

Matthew Oakley: Up to the task of evaluation and taking action? I am not necessarily saying that this should be incumbent on the FCA. The Treasury and the Department for Work and Pensions are highly invested in this. It needs to be a joint programme of work between those three bodies to work out what is happening, and we need some serious consideration of how it will happen. We need to start collecting data now that say how consumers are engaging and behaving, and what they think of the guidance guarantee and the market once they hit retirement. That needs doing; otherwise, we will end up in a situation in five years' time where we basically do not know what has happened, and that is a real worry.

Q191 Gregg McClymont: On that point, there was a very good question asked the other day—I cannot remember by whom—around the sharing of information between the various agents in the guidance process. It was asked whether Citizens Advice and TPAS in particular had shared IT systems, to allow them to call up previous engagements with the guidance process. The answer given was no, as far as we are aware. Is that the kind of area where we will have to see movement quite quickly?

Matthew Oakley: I would hope so. That talks to the point I made earlier around having a combined view of the person's investments, savings, and pension pots. You could imagine in due course that each of those guidance providers could have access to those with permission from the consumer. My worry is around consistency across the country between providers, and between face-to-face, online and over the phone. There is a worry that consumers will face detriment because of the choice of where they go or where they live, not because of their poor choices. For me, it comes down to ensuring that we have the information available to say, "It is working here, but not there," and to take action as soon as possible to rectify that.

Q192 Gregg McClymont: Let me ask about CDC, the larger part of the Bill. I want to try to put this as simply as possible, because there is a lot of ground to cover. What is the fundamental problem with individual DC, which collective DC has the potential to solve?

Tim Sharp: We think it is fundamentally inefficient. You have got lots of little pots of money that are being invested. You have efficiencies through having one big pot of money. I think that feeds through to the investment choices that can be made. When you have collective schemes with lots of members, you can invest in a broader range of diversified assets and, hopefully, have a smoother growth in the pot.

The final part of it is around the retirement income. CDC provides the ability to share longevity risk across a big cohort of people, rather than the expensive process of either draw-down or buying an individual annuity, which you would have to do under an individual DC.

Q193 Gregg McClymont: Dominic or Matthew? Only if you wish to.

Dominic Lindley: I would absolutely agree with those. It provides greater certainty to consumers and greater efficiency, and takes away the burden from consumers of making complicated decisions. I have seen market research around the new freedoms where consumers say they want freedom and choice, but a substantial proportion also wants a secure income for the rest of their lives. Many do not want to make complex choices. At the same time as we are introducing a welcome additional freedom, we have to ensure that that option is there for people who are not willing or able to make those complex and very difficult decisions. It is very difficult to decide exactly how much you want to draw out of your pension each year, and how long it is going to last.

Q194 Gregg McClymont: With the Chair's permission, can I ask another question? If anyone else wishes to come in, please stop me. There are different forms of CDC. There was an interesting exchange between Richard and Nigel and previous witnesses around how one puts into practice making CDC work, and whether the pooling of risk is intergenerational or within one generation. What do you think in reality is likely to be the form of collective defined contribution that first emerges after this Bill?

Dominic Lindley: One thing to point out is that there are already schemes that involve some risk-sharing and smoothing. They are called with-profits funds. They have been around for many years. Some of them have not provided particularly good outcomes, partly because, as Tim said, they were run by insurance companies that put shareholders' interests above the interests of consumers. Some schemes smooth out the return over time. Again, somebody will have to provide capital to back those schemes, or you will have to charge the first lot of members a bit more to build up that fund. That is a big question that still remains to be answered.

Q195 Stephen Hammond: Probably my question was asked with more skill and guile by the hon. Member for Cumbernauld, Kilsyth and Kirkintilloch East. I was listening to some of the interchanges, particularly the comments from Mr Lindley about the FCA. I would be a bit blunter than the shadow Minister and say that I rather detected from your comments that, given its preoccupation with its regulation of banking, you had a low level of confidence in its ability to regulate in this area.

Dominic Lindley: Yes. The pensions regulator has the right ideas, but it lacks the capacity, the powers and the funding, and it does not cover contract-based schemes. The FCA has been slow. I will give you one example. Consultancy charges could have resulted in people being charged very high amounts of money when they were auto-enrolled. I was warning about risks of high charges for years, and the FCA did not take any action. It took the Minister to intervene and ban consultancy charges. The FCA still did not do anything about them. At the moment, the jury is still out. I really worry that it will spend a lot of its time designing a leaflet to go into the pack that consumers get at the time. While it is important, it will not provide that second line of defence, that strong governance and that cap on charges that consumers will need to protect them.

Q196 Stephen Hammond: With regard to your very last comment about with-profit schemes, it would be fair to say, would it not, that a number of with-profit schemes have been highly successful and have generated significant benefits to the members of those schemes? It is important that we put that on the record. Your comment rather suggested something else.

Dominic Lindley: Certainly a lot of with-profit schemes, and even with-profit schemes that were supposed to be run in the best interests of members—Equitable Life, for example—made a big mistake in not reserving for the guarantees that they had offered to members, and then got into significant difficulty. Other with-profits funds such as Prudential have delivered very good long-term returns with smoothing. The real difficulty came when the initial company that set up the with-profits fund sold it on to a consolidator who started to run the fund more in their interest than the interest of consumers. As those funds are closed to new members, they are not interested in attracting new members, which pushes down the performance. Funds such as Prudential are still open and interested in attracting new members.

Q197 Richard Graham: I am conscious that time is running out, so this will be a very quick soundbite. On that last point about with-profits schemes, these were totally inexplicable to the consumer. They made huge mistakes and they blew up. Do the three of you really feel that they can be resurrected in the way that people can understand, and without the risks of them blowing up?

Tim Sharp: The point at issue here is around scheme governance. If it is run by trustees operating entirely in the interests of scheme members, then a lot of the problems we saw with with-profits should be avoided. There are more potential conflicts of interest in contract-based schemes, but the moves to place obligations on managers—

Richard Graham: We have one minute.

Matthew Oakley: I agree with that. The only thing I would add is that consumers need to understand what they are getting into. These schemes are by their nature welcome, in terms of innovation and delivering more certainty in retirement, potentially, but they will be complicated. Consumers need to understand that.

Dominic Lindley: With-profits funds are another example of failed FCA regulation. The FCA required with-profits funds to set up what it called with-profits committees to provide some kind of independent judgment. Of course those with-profits committees could include people from the insurer executives, including executives from other insurers. The FCA is really repeating those mistakes when requiring contract-based companies to set up so-called independent governance committees. The FCA really has not learned its lesson from with-profits funds. The other issue is that the FCA allowed proprietary companies to raid the with-profits funds to pay compensation when the company mis-sold a policy.

The Chair: Order. I am afraid that brings us to the end of the time allotted for the Committee to ask questions. I thank the witnesses on behalf of the Committee for their evidence.

Examination of Witnesses

Chris Curry, Dr Ros Altmann and Jane Vass gave evidence.

12.16 pm

The Chair: We will now hear evidence from Chris Curry, director, Pensions Policy Institute, Dr Ros Altmann, pensions expert, and Jane Vass, head of public policy, Age UK. For this session we only have until 1 pm. Would the witnesses please introduce themselves for the record?

Chris Curry: Good afternoon. My name is Chris Curry. I am director of the Pensions Policy Institute.

Dr Ros Altmann: Good afternoon. I am Ros Altmann. I am an independent adviser on pension issues and the business champion for older workers.

Jane Vass: I am Jane Vass, head of public policy at Age UK.

The Chair: Thank you. I will now take questions from Members.

Q198 Nigel Mills: Perhaps we will start with you, Dr Altmann. Could you talk us through what you think the guidance guarantee could achieve to help protect people in choosing their retirement income?

Dr Ros Altmann: Certainly in theory the guidance guarantee is something we have needed for many years. We have needed consumers to have somebody to talk to, to discuss the options they face at retirement and what to do with their pension pot. Clearly, with the reforms we have had there will be an increase, potentially, in the options available. Until now you had the binary choice. When you have a DC pot you either buy an annuity or an income draw-down product. There is likely to be a wider range of products.

However, even with just the annuity and draw-down choice, this was not a simple decision. Many people, sadly, did not understand what different types of annuities were available and the industry simply offered people what it called a standard annuity. That was wholly unsuitable for many of the people who bought them. Had they had guidance, they would have had a much fairer chance of understanding what type of annuity to buy, not just focusing on getting the best rate for the wrong annuity but actually getting a good rate for the right annuity.

I would hope that the existence of guidance will ensure that more people are able to make a better informed decision about what is best for them to do with their pension fund. For many people, the decision might be to do nothing at the moment and leave the money invested. However, I am concerned that there is a serious risk that not enough people will receive the guidance, even though it is on offer, certainly at the beginning because this is all very new. I would very much like to see additional safeguards to protect consumers, beyond relying on the guidance that we already know many people may not take up.

Q199 Nigel Mills: What would those additional safeguards be?

Dr Ros Altmann: I would like to see—it is something we have needed for many years—an obligation on whoever is selling somebody a product at retirement to comply properly with the Treating Customers Fairly rules that already exist. I fear that the regulation of this sales process has failed to understand how consumers think, how they work and what they need. In theory, you have TCF rule No. 1—consumers must be confident that they are dealing with someone for whom the fair treatment of them is central—but that does not necessarily seem to have applied in the past. Rule No. 2 is that products are designed to meet their needs and are "targeted accordingly". Once again, I do not see how selling a standard annuity has really complied with that in the first place. I would certainly like to see something tightened up there. Rule No. 3 is that consumers are "provided with clear information" so that they understand what product they are buying.

In my view, the sales process has consistently failed the customer from the TCF angle. We might address that by requiring providers to ensure that products being bought are suitable. They cannot possibly know whether an annuity sold to someone is suitable unless they ask some relevant questions. There is no requirement to ask someone, "Have you had cancer? Have you had heart trouble or diabetes?" There are people with terminal cancer who have bought a standard annuity which assumes they have a healthy life expectancy. All it would take is a question of that nature before the product was sold. It is so important because annuities, once sold, are pretty much irreversible. I would call on the FCA to ensure that providers are required to treat customers properly and fairly, and to have this safeguard so that if you do not get the guidance, someone will at least take notice of your circumstances when you buy a product and help you with what questions to consider before committing.

Nigel Mills: Okay. Thank you.

Q200 The Minister for Pensions (Steve Webb): My first question is for Chris. We will no doubt discuss the issue of governance, and I think you heard the argument this morning that, "The only good governance is trust governance. Trust good, contract bad." Indeed, so unsatisfactory is contract-based governance according to that argument that CDC should only be set up under trust. Do you think it is as stark as that?

Chris Curry: It is always difficult to rule out any particular form of governance. Internationally, especially in the collective DC area, most schemes tend to be set up on a trust basis. That is mainly because it seems more obvious; someone is acting in the interest of the members. One really important feature of CDC is strong governance and someone acting on behalf of all members with a clear, single responsibility to that group. The trust-based model lends itself to that. However, I would not say that is impossible in any other form of model. As we heard, there are some well-governed with-profits funds which have operated on a contract basis as they go through. I do not think you could explicitly rule out a whole class. You would have to be very careful about how it was set up. What is really important is the alignment of interests. In any type of collective arrangement, you would need someone within that scheme with real power and authority who is acting in the members' best interests. At the moment, that generally operates very easily within a trust-based system, but you would not have to exclude all other forms to ensure it definitely happened.

Q201 Steve Webb: Thank you. Ros, you were very supportive of the new freedoms the morning after the Budget. Lots of people contact you, and I am guessing that you have been contacted by people who missed out. It would be interesting to get a sense from you of how big this issue is for people who locked into annuities before the changes came in. How strong is the case for finding some way of addressing their concerns?

Dr Ros Altmann: I have had a significant number of e-mails and communications from people who locked into annuities in the year or two before the changes were announced and who desperately want to undo the deal. That is sometimes because they are very ill or, having seen the headlines, have suddenly realised that an annuity was not an appropriate product for them at all or they bought the wrong type and want to change it. I do feel very sorry for them, having watched the annuity market as it developed over the last two or three years, and tried to warn of the poor value that many people suffered as a result, or the lack of any protection to ensure that the annuities being bought were actually suitable for the people buying them, and that they even needed to buy one at the time. Many were still working and they just thought, when they got their letter from their pension company saying that they had reached pension age, they had to do something. In many cases they did not. Sometimes they might have been penalised if they had not done so, but in many cases that would not apply either.

So I think if there were a way in which annuities could be undone it would be very popular among a number of customers, and I have even had many people suggesting to me they do not mind if they have to pay a penalty. If they have received back X pounds, they do not mind having to pay or being assumed to have received somewhat more than they have actually had—just to get the balance of their fund back. They have urgent reasons why they might want that; if they had only known.

I understand, too, that it is very difficult for companies that have sold a product like this under contract, which is completely irreversible, and have made business plans on that basis, to consider how to unwind the deal, but I would imagine it is not impossible if the will is there; and especially if there are people who have clearly been sold an unsuitable annuity, I would think the case is very strong for looking into that.

Steve Webb: Thank you.

Q202 Stephen Hammond: May I ask three questions? First, given the new rules on annuities, is much of the benefit of this Bill going to be taken away, because the new rules are really much more important to the consumer? If not, what do you estimate the take-up of collective DC schemes to be?

Dr Altmann, when you spoke initially about the guidance guarantee to one of my colleagues, a moment ago, you expressed some hope that it would be taken up. I suppose I am looking for a confidence level, and what we should do to make sure that confidence level is better.

Thirdly, I take your point about the end process where you do income draw-down, but could you not argue that, through the life, a CDC is effectively less transparent than an ordinary DC scheme to the average member? It may or may not be more transparent if you have the right trustees in place, but then that begs the question whether we have enough people to be the right trustees, and whether those trustees choose to give that information to the members of the scheme. That is to any and all of you, I suppose.

Jane Vass: I will be brief, because I think on your point about collective schemes and pension schemes in general—in the auto-enrolment world, it is not actually the consumer's choice; so that, I think, changes the dynamic. It is very much the employer's choice, and you need to look at how the whole system hangs together; so one of the questions would be how it works if you move from scheme to scheme.

In terms of the take-up of guidance, we would certainly hope that it would be taken up, but I think we have to recognise that at the starting point we would need to move it much further down the line; so I think that having a really highly regarded system that is not too restrictive—that is personalised—so that people get that customer interaction they are looking for, will start to build consumer trust in it. Does that help?

Dr Ros Altmann: I think you are correct that the new pension freedoms do take away some of the attraction of a kind of hybrid scheme—defined ambition, collective arrangements—because the individual may at the end of the day decide they want to take their pot; and most CDC schemes, and certainly the collective defined contribution schemes, which still have an element of risk-sharing, tend to rely on the money staying in rather than disappearing at the point of retirement.

Nevertheless, maybe one could look at what I have called, to distinguish it from collective DC, pooled DC, which is a collective arrangement but only so far as the assets are pooled. One of the big problems we have at the moment is that for the accumulation stage we are trying to help people one by one. That inevitably means we do not capture the same kind of economies of scale. We do not necessarily have access to the same range of asset classes that you might have with a big pool of assets such as we currently have for DB schemes. I would also argue that the investment approach for defined contribution in the UK is significantly far behind the investment approach that is now prevalent in defined benefit, perhaps to the detriment of the members. Generally, DC investments are run as DB used to be run many years ago; DB schemes and trustees have learned quite a lot since then. Having a bigger pool of assets that can really be invested for the long run I think still has merit, even if we then allow people access to a pot at retirement, and do not have the same protections on the ultimate pension benefit payout but maybe protections on the Government pot that they get at the point of retirement.

From the point of view of looking at what an employer might choose to do, it is difficult to see them, in the private sector, signing up to the really quite strict restrictions on defined benefit as they are outlined in the Bill. In terms of the shared risk, you could see that at least some private sector employers may be attracted to that. How we make it work better for members is an important issue, and I do not think allowing them total freedom at retirement necessarily undermines that case.

On your second question, of course I hope that the guidance will be taken up. I have done some survey work and others have, too, to see what people are currently saying. In our recent survey, about 56% suggested they would like to take up face-to-face guidance, but the critical part for me is that they have to know it exists and have to understand what it is, so in a way section 333B of the Financial Services and Markets Act 2000, which would be inserted by the Bill and which says that the Treasury "must" ensure people have access to guidance, is right, but then it says only that the Treasury "may" increase awareness or do research or promote the guidance in some way. I would prefer to see "must", certainly at the beginning, so that it is essential that this is promoted.

We are doing really good stuff. If we get this working correctly—I hope we will; there is a significant likelihood that we can and certainly we should be able to—people need to know about it. They need to have confidence. I think that is why we have chosen the partners that we have. We want people to trust it. Clearly, there is a lack of trust in the industry. I am talking about the marketing and promotion of this service. If it really is good, let us shout that from the rooftops and get people to come and take part in it.

Chris Curry: To start with the first question and collective defined-contribution or defined-ambition schemes and whether what was announced in the Budget—the freedom and choice—undermines that, the first thing we have to bear in mind is that we are not really clear yet on what the implications of the freedom and choice changes will be. We do not know how many people will be taking lump sums, how many people will want to be staying invested and drawing out periodically during their retirement, and how many will still be interested in securing an income through annuities at one point or another. The international evidence is mixed: how people actually react depends very much on the environment in which the system operates and the tax advantages and the treatment of annuities.

We also need to bear in mind that a lot of focus around the Budget changes relates to next April, when everything comes online. The collective DC agenda is talking about a much longer time frame and a very different group of people. That builds into where the automatic enrolment agenda has come from. We know that some people who reach pension age and will be drawing down pensions from April onwards have been automatically enrolled, but the vast majority of people who are automatically enrolled will not be reaching an age at which they take money out for another 10, 20 or 30 years. By that stage, we might find that what people do when they reach that age is very different from what people who reach pension age now do—their characteristics will be different and they will have had very different types of pension arrangements with them. They will probably have spent a lot of time in DC, whereas people at the moment might have some DC, some DB. Housing wealth might also be very different.

We have to bear in mind that very different time frames are involved here. With that in mind, we can still see how something that is not defined benefit—I agree with Ros that outside the public sector there is not going to be much appetite for carrying on with that. There will be some—it will not disappear completely—but I do not think that it is likely grow in the near future. The defined contribution issues are around whether that is the right level of risk for individuals to be taking. Something that tries to share that risk in whatever way, whether with an employer or an insurance company, or between other members of that pool or between generations, probably gives people more of an opportunity to have a little bit more certainty and potential stability in what they might be able to achieve.

It is also important to bear in mind that it is not necessarily just a stark choice between DB, DC or DA. We could envisage a system in which all of those are operating and, in fact, to preclude one type or another would be to limit options, which goes against the freedom-of-choice agenda, which is trying to give people more ways of operating that.

On the transparency issue, there are always different levels of engagement and different ways in which people view arrangements. You could argue that although people in DC schemes and automatic enrolment are given lots of information, they do not necessarily understand how it works. The vast majority of them are in a default fund and the vast majority of them will not be thinking about the workings of what is going on, so a lot of the transparency issue is down to communication and how people understand what they are entitled to and not entitled to, what they will get and not get, rather than necessarily the underlying workings of the scheme. There is a big challenge for all types of schemes to be transparent about what people can get and can expect, and the risks and uncertainty around that.

On the guidance issue, I think the guidance guarantee is a recognition that individuals will need help. At the moment, it is focused clearly on the point of retirement, when people will need help to decide what to do. As Dr Altmann pointed out, we have known for a long time that people have needed help there and have not necessarily had that help. The real challenge, as recent research has shown, is to get people to take advantage of that guidance. One of the most telling parts of the discussion over the past 15 years in pensions has been the introduction of automatic enrolment, because we know that people do not engage, even if it is in their own best interest. With a guidance guarantee, a similar thing could happen. It is in people's interest to be able, free of charge, to speak to someone who can help them to make what is an important decision for them.

There are conflicting views on that. We have had evidence about asking people what they planned to do, if they would like to take advantage of this when offered to them, and of course most people say yes. We have also had pilot schemes where people have had the opportunity to take advantage of it, but less than 2.5% of people have taken it up. So there is a real challenge in making sure that people get the help that they need, but the introduction of the guidance guarantees a very good first step in helping people.

Q203 Gregg McClymont: Jane, can I ask you something first? I imagine that Age UK has a particular concern around the impact of changes in the pensions landscape on older individuals. Previous witnesses discussed to some considerable extent the issue of how one gets safeguards into the processes around guidance, particularly with the new draw-down products. What is Age UK's sense of how robust those safeguards are as things stand? In what direction might they travel?

Jane Vass: One of the points that we picked up in responding to the FCA on the retirement reforms in September was that there is a gap in what happens between someone going to the provider and taking the advice. Also, what happens when someone does not take advice? The truth is that we simply do not know how many people will. We hope that people will, but we think that consumer-facing guidance needs to go hand in hand with industry-facing regulation. You cannot put all the responsibility on the consumer, but I think we need to delve down carefully into where the detriment is.

If somebody comes to the provider and says, "I want my money and I want it now," I think the provider absolutely must say, "Have you taken advice? Are you aware of the impact on your tax situation?", which I suspect might be quite a useful question to ask people and encourage them to go back to guidance—and indeed, try to understand some of the reasons why they are so desperate. Is there a debt situation involved, in which case they should definitely be referred back to debt advice?

If somebody is considering rolling over with the existing provider, again, I think we need safeguards there. I am a bit anxious about the concept of just asking people a list of questions and getting them to tick a box, because we know in the past that sometimes less reputable providers have used that as an opportunity to get people to tick the box and then say, "It wasn't me, guv. They said they were okay." In that case, I think we would be looking at building sensible defaults into the system. You may say it is a system that is not set up for defaults, but actually, any provider who limits choices is, in a way, providing a default, but also providing straightforward choices.

The FCA will need to be active and vigilant and needs to be talking to companies now about what their plans are, challenging them on how that will meet the suitability requirements and considering the products. Are products being brought in with irrevocable terms and conditions that will make it very difficult for people to get out of them? For example, there needs to be exploration and perhaps some work on exit fees and any restrictive terms like that, and if that turns out to be a problem, it will have to act fast and, potentially, consider some form of quality assurance scheme—caps on charges, that sort of thing. It will have to move quickly, and in the meantime, the guidance is a really vital back-up.

We would hope to see a programme of research, and we agree with Ros that the Treasury should be required to carry out research to ask, for example, "Who is taking up the guidance?" and, "If they are not taking up the guidance, why?" and to track different forms of engagement—so, to test the box-ticking approach of people who come to them against different sorts of questions and to use the behavioural knowledge that we are gaining, to find the best way forward.

Q204 Gregg McClymont: Does it seem peculiar to you, Jane, and Age UK that just as the nettle is beginning to be grasped on charges and quality criteria in the "building the pot up" phase, that we are now moving into a greater emphasis on draw down, without those same safeguards?

Jane Vass: It is a real concern that the products that come in will be expensive and complicated. In the past, innovation has not always worked in the interests of consumers—consider structured capital at risk products a few years back—so we think that it is important to learn from that. For example, we would be very concerned if people were moving money unnecessarily out of a charge-capped fund into a very expensive, complicated fund, so we do need to keep a lid on charges and look across the industry at what best practice is.

Q205 Gregg McClymont: Ros, you addressed some of this in your response to questions from other members of the Committee. I noted down that you were calling on the FCA to ensure proper compliance with treating customers fairly. We know that in the wider contract pensions space, that criteria has not always worked effectively when put against the pressure to deliver for shareholders. How would you like to see the FCA make that commitment manifest and effective for savers? What specifically should it do to ensure that customers are treated fairly in this new draw-down space?

Dr Ros Altmann: Consumers have been left in the dark and at the mercy of the providers for years. Providers must be required to know who they are selling something to before they sell it. In other words, I believe they must be required to ask some fundamentally important questions of whoever it is they are selling a product to, whether or not that person has had guidance, but particularly if they have not had guidance. The problem is that we do not know how many people will take up the guidance, so we have to assume that a customer coming along may not have had guidance and therefore needs this extra safeguard.

The questions need to go to the heart of the product being sold. In other words, "Have you explored the 'do nothing' option if you are still working?" "Are you still working?" is a very important question. "Do you have other pensions?" is another very important question. The provider who is selling a product does not want to know that, because they want to sell you the product, but the product is not necessarily what the customer needs or what is best for them.

"Have you got any serious health issues?" is a very important question, which nobody is required to ask. If you are about to sell someone a standard annuity, they need protection against that. They need some question that identifies them as having a health issue, which would mean the provider could not then say that selling them a standard annuity that assumes they are healthy was appropriate.

"Do you have a partner—an unpensioned partner—who needs covering?" is also a very important question that needs to be asked before somebody buys a product that does not cover a partner. There is a list of questions, which is not that long and which providers should always have asked and should always have been required to ask but have not asked, and we could now ensure that they do ask them before selling a product.

It would be ideal if the default option was a "do nothing" option, so that you have to make a positive choice to do something. The alternative is to leave your money there if you do not need it. Then, if you really do need it, you have to engage with that choice, but if you do not need it, there is a default that says, "Leave it to grow," as we have been trying to do. I mean, we have put so many billions of pounds into tax relief for pensions; we just do not want to see it wasted any more at the point of retirement, if we can possibly help it.

In addition, I would like to see trustees of pension schemes—who we have not talked about yet, because they are a TPR issue rather than a FCA issue—also being required to take care of their members at the point of retirement, in a way that they have not been. Until now, it has apparently been an adequate discharge of their duty just to send members to an annuity-selling service, without ensuring that they have got the right type of annuity. Perhaps there needs to be more emphasis placed on trustees to ensure that members get the guidance, for example. That is something that trustees, who are usually trusted by their members, could ensure happens.

We need to put safeguards in place, which the FCA and the Pensions Regulator can require, that ensure that—much more effectively than we have done in the past—the products that are being sold to somebody have a good chance of being suitable for them. And of course we must then ensure that the FCA follows up to check that that is actually happening and that, if there is an unsuitable sale, it is not just a case of, "Well, sorry, you mis-bought. It's nothing to do with the selling process," which appears to be where customers fall down at the moment. The customer goes along and the provider says, "Well, you signed the form. You had your wake-up pack with all the information." Well, if you have ever looked at these wake-up packs, they are guaranteed to put you to sleep; nobody can understand the language being used in them. If we had a one-page form that says, "This is the size of your pension fund, and this is a particular feature of your fund," it could be standardised. It has never been standardised and therefore people just do not have a chance to understand it properly and need protecting.

Chris Curry: I would like to concentrate on the group of people who we know are not really going to engage, and who probably will not take up the guidance or advice. I think both Jane and Ros have mentioned it. There is a strong case for very strong defaults in any system. What we know from our studies of behaviour of people coming up to retirement and people who have taken up a guidance guarantee when offered, and from survey evidence of when people think they are likely to retire and when they will decide about it, is that people leave it late to make decisions. They generally follow the path of least resistance in what they want to do. I think there is a strong case for defaults that start to kick in maybe 10 or 15 years before retirement.

The way that a pension fund is invested and de-risked in the build-up to a particular point when someone may or may not think they are likely to retire is important. A default strategy that can cope with uncertainty, given that we know that people may still have to take late decisions as to whether they carry on working or not, depending on how well their fund has performed and such issues, is really important. For the vast majority of people the default situation in a relatively small number of very big auto-enrolment schemes will be critical.

What happens with NEST, the People's Pension, Now, and Legal & General is going to have a big impact on a large number of people. Those defaults need to be designed in such a way that they can cope with flexibility. If you do not know exactly when people are going to start taking their money or if they are going to take it as a lump sum or if they are going to want to buy an annuity with some of it or keep it invested, something that can cope with that is never going to be the best outcome for any particular individual, but is not a bad outcome for anyone. That is an important part of what we are looking at here.

It is also important to reiterate something I mentioned earlier. This is not something that it is necessarily possible to get right for April. In fact, whatever you have in place in April might well not be what you need to have in place five, 10 or 15 years' later. It is important to see this as not just a one-off change in the market and everything changing. This is the start of an evolutionary process where providers are going to have to be very aware of who are members of their schemes and what they are likely to want to do in future.

Q206 Gregg McClymont: Thank you. Chris, the Minister asked you about the debate over contract versus trust. I think it is fair to rephrase the Minister's question as, "Have there been some circumstances and times and places where contract has worked better than trust in this space?" On balance overall, given the challenges we are talking about around this new world of draw-down, in your judgment what system of governance is necessary and most likely to deliver a decent outcome for all savers?

Chris Curry: It is difficult to say that one is always going to be better than the other. The key things are to have a strong governance framework and alignment of interests. Where you have that in a trustee framework that is very clear-cut. You have trustees with a fiduciary duty. Their role is to get the best for their members.

What I was trying to say earlier was that that is not impossible outside of a trust-based framework. You and the people you have involved just have to work hard at it and be incredibly clear. In some cases, it does come down to having the right people doing it. You can get good trustees and bad trustees. There are good people in the contract world and providers in the contract world who do not put as much emphasis on this. The key things are having a clear alignment of interests, a very strong governance framework and making it obvious what people are doing and why. As you said, that might be easier in a trust-based world, but it does not mean it cannot happen in a different world.

Q207 Gregg McClymont: In your judgment, on balance it is more likely to be easier to achieve in a trust?

Chris Curry: It has happened more often internationally in a trust-based system.

Q208 Gregg McClymont: I like empirical evidence.

Chris Curry: So do I.

Q209 Richard Graham: We have only six minutes left, so I would be grateful if you could all be swift in answering. Jane, did Age Concern consider offering yourselves as people who might provide this guidance? Is this not something that naturally in future would be an area for you to try to take forward? Secondly, in terms of your current clients, many of whom are our constituents, what issues would you like to see covered specifically in the guidance?

Jane Vass: Age UK did express an interest in being involved, but we thought the right fit for us would be in supporting the delivery through some form of triage service, and working with experts such as the Pensions Advisory Service to help people to prepare for the guidance session, doing the nitty-gritty things like keeping track of their paperwork, and then helping people afterwards, and also providing the wrap-around service and links to other information and advice that they might need. In terms of our current clients and the guidance that people need, it is very nitty-gritty stuff. You cannot make truly informed decisions unless you also consider issues such as your debt, your tax position, your family circumstances, your housing, and your potential long-term care needs and suchlike.

Q210 Richard Graham: That is very helpful stuff. Chris, a more philosophical one, because you produce papers on all sorts of thoughtful issues. The changes that have come through from both DWP and Treasury suggest that we are gradually moving in the direction of a greater focus on savings and a lesser focus on pensions. What do you think the implications of that are, as far as you can concisely put them in about one minute?

Chris Curry: One minute? Thank you. What we have seen is a reduction in the constraints around pensions, which makes them look more like savings in some ways. However, at the moment, there is still a tax advantage attached to pensions, which is greater than that placed on most savings. I think there is a question for employers and employees about what they do as part of pension arrangements. We still do not know exactly what is going to happen from April, and it might be that there is still a part of pension income that finds its way into securing a retirement income, which is probably a good thing and is really the aim of what is going on—the reason for having pensions.

I think this area will probably evolve further, and the more that the lines between savings and pensions become blurred, the more difficult it is to distinguish what the role of employers and the Government is in trying to provide support for those different types of saving.

Q211 Richard Graham: Do you think the big challenge will be about a source of guaranteed income?

Chris Curry: It will be interesting to see if people still have faith in annuities, given the reputation that they have had, which I think is difficult because there have been some very good annuity products available for people if they have been able to get the right guidance and advice to find them. Most of the research evidence suggests that people still want security in retirement and still want at least some element of fixed income, be that through an annuity or through a regular draw down, or even potentially through a collective DC arrangement. The challenge is to allow people to do that as much as they want and need to do it, but also allowing them some flexibility if they have anything in excess of that.

Q212 Richard Graham: Thank you. Ros, lots of things, really. You talked earlier about perhaps having a default that allowed people's pensions to run on and then they would decide when they wanted to use them. The argument against that is the one about knowing what your income is going to be. For those people who do not have many other savings—individual savings accounts or whatever—what are they going to live off if they simply leave their pension in there to accumulate and grow once they have stopped working?

Dr Ros Altmann: Going back to the philosophical element, which is an important one, perhaps we should accept that the old idea of a guaranteed income in retirement, as we have previously thought about it, is not quite so appropriate any more. The big issue that many people are going to face is funding long-term care, and a guaranteed income will not help you with that. I therefore feel that the changes that we have now could make pensions become much more of a family savings pool.

Q213 Richard Graham: Savings for care?

Dr Ros Altmann: If you discourage people from spending the money altogether at the point of retirement, which is of course what an annuity does—it is in exchange for a stream of income, but nevertheless the money is all gone—there is a much more significant likelihood that at least some of that money will remain there for longer. The removal of the 55% tax charge on inherited funds, plus the ability to be more flexible with what you do with your pensions—

Q214 Richard Graham: And because it can be handed on, people might think of it more as a legacy?

Dr Ros Altmann: It suggests that the last thing you would want to spend, if you understood how these things worked, would be your pension. If you have ISAs, you spend those first. If you have a house, even, you use that money first. Keep the pension there. You could argue that the original idea of pensions was really to fund savings to look after you when you cannot look after yourself.

The Chair: Order. I am afraid that brings us to the end of the time allotted for the Committee to ask questions. On behalf of the Committee, I thank the panel for their evidence.

Ordered, That further consideration be now adjourned. —*(Dr Thérèse Coffey.)*

1 pm

Adjourned till this day at Two o'clock.