Response by TISA to:

Second State Pension age review: independent report call for evidence

Renny Biggins, Head of Retirement
renny.biggins@tisa.uk.com – 07802 324962

About TISA

The Investing and Saving Alliance (TISA) is a unique, rapidly growing membership organisation for UK financial services.

Our ambition is to improve the financial wellbeing of all UK consumers. We do this by focusing the convening the power of our broad industry membership base around the key issues to deliver practical solutions and devise innovative, evidence-based strategic proposals for government, policy makers and regulators that address major consumer issues.

TISA membership is representative of **all sectors of the financial services industry.** We have **over 240 member firms involved in the supply and distribution of savings, investment products and associated services**, including the UK's major investment managers, retail banks, online platforms, insurance companies, pension providers, distributors, building societies, wealth managers, third party administrators, Fintech businesses, financial consultants, financial advisers, industry infrastructure providers and stockbrokers.

As consumers, the financial services industry and the economy react to and recover from the effects of the pandemic, the importance of the three key pillars of work that TISA prioritises has never been more apparent:

- **Strategic policy initiatives** regarding the financial wellbeing of UK consumers & thereby enhancing the environment within which the industry operates in the key areas of **consumer guidance, retirement planning, later lifetime lending, vulnerable customers, financial education, savings and investments**.
- TISA is recognised for the **expert technical support provided to members** on a range of operational and regulatory issues targeted at improving infrastructure and processes, establishing standards of good practice and the interpretation and implementation of new rules and regulations covering **MiFID II, CASS, ESG/RSI, operational resilience, Cyber Risk, SM&CR** and a range of other areas.
- **Digital transformation initiatives** that are driving ground-breaking innovation and the development of industry infrastructure for greater operational effectiveness and revenue promoting opportunity for firms. TISA has become a major industry delivery organisation for consumer focused, digital industry infrastructure initiatives – **TISAtech** (a digital marketplace that brings together financial institutions and FinTechs for greater collaboration and innovation) and **TURN** (TISA Universal Reporting Network – a digital platform providing a secure data exchange for financial services using blockchain technology) – alongside projects **Digital ID** and **Open Savings & Investment**. This reflects TISA's commitment to open standards and independent governance.

Executive Summary

TISA welcomes the opportunity to respond to the DWP call for evidence - Second State Pension age review: independent report call for evidence.

Our response is based on some important expectations that we set out below:

- **There will be no cut to pensions in payment**
- **There will be no retrospective changes made to entitlements already accrued**
- **State Pension entitlement will continue to be funded through National Insurance (NI) contributions.**

It is crucial that the State Pension Age is reviewed periodically to ensure it remains fair and sustainable against a constantly changing landscape. Given the various components which should be included in such a review, there needs to be clear definitions for 'fair' an 'sustainable' to enable the review to be objective and generate equitable outcomes for individuals, irrespective of economic and demographic factors which largely remain out of Government control.

When reviewing the State Pension, we need to also consider other national pension systems that are in place. It is common among OECD countries for total pension provision to be made up of several components or pillars, with different funders, benefits, retirement ages and contribution structures in place for each.

For UK, the other pension system we have in place is Auto Enrolment (AE). As participation amongst eligible employees has exceeded 85%, this is now considered by OECD as a quasi-mandatory scheme. We should ensure that all reviews and changes to the SP take in to account the overall retirement income targets that are deemed appropriate and the impact this has on AE's ability to deliver on the income level that will be required from private pension provision.

From a workplace pension perspective, we have moved away from retirement being defined by a single date with DB to typically, a flexible phased retirement approach with DC. We believe a small amount of the flexibility associated with modern pension systems should be integrated into the SP. It is currently possible to defer taking SP benefits to secure a greater level of future benefit - either through election or as a default in the event of a claim not being made. Given that personal circumstances come in all shapes and sizes, it would be appropriate to consult on a national approach, enabling limited early access flexibility. Although this option could be simply communicated, many will not be equipped to make such a decision and as such, we believe anyone wishing to claim early should evidence they have received regulated advice or attend a mandated MaPS guidance session.

We would be pleased to discuss any aspects of our full response with you in more detail.

Question responses

3.1. Intergenerational fairness:

As people are living longer, how do we ensure the costs of State Pension are shared fairly across generations?

Whilst it is possible to ensure that the State Pension (SP) retains long-term fairness across generations, the increasing costs due to an ageing population raises the question on how this is funded. This will inevitably involve a trade-off, which translates into a corresponding reduction in other areas of government expenditure and/or the generation of more revenue through the introduction of higher or new taxes. This highlights how sensitive the SP is to political intervention.

There are a significant number of political, economic and demographic factors in play which influence SP decisions. Notably, as the number of pensioners is increasing faster than the number of working age people, it means for the pay as you go system in place, that the rising cost of SP payments need to be met from a reducing income stream.

It needs to be universally acknowledged that the fairness of costs can only be measured against the current and expected economic environment on which decisions are based. Importantly, whilst consistency needs to be achieved in terms of fairness, this does not necessarily translate into consistency of costs and the level of benefits paid out. A 'fairness' definition needs to be clearly defined to ensure that future reviews and proposed change can be assessed against this measure.

When reviewing the SP, we need to also consider other national pension systems that are in place. It is common among OECD countries for total pension provision to be made up of several components or pillars, with different funders, benefits, retirement ages and contribution structures in place for each.

For UK, the other pension system we have in place is Auto Enrolment (AE). As participation amongst eligible employees has exceeded 85%, this is now considered by OECD as a quasi-mandatory scheme. We should ensure that all reviews and changes to the SP take in to account the overall retirement income targets that are deemed appropriate and the impact this has on AE's ability to deliver on the income level that will be required from private pension provision.

We should also be mindful of the trends occurring in the private sector over recent decades, notably the sharp decline in Defined Benefit (DB) provision. In the latest ONS published data for the 55-64 age group, the median combined DB and Defined Contribution (DC) pension wealth was £107,000 (with a heavy skew towards DB - DB £186,600 and DC £35,000). This is well below the pot size that a consumer requires to purchase an annuity that would deliver a moderate living standard in retirement. According to a recent PLSA study, an individual needs £20,800 p.a. (net of taxes) to achieve moderate living standards in retirement requiring an annuity purchase of £270,000 – which would then deliver a net income of circa £20,800 (inclusive of a full state pension). We can expect the combined median to reduce as the ongoing reduction in DB will not be adequately offset by increased DC wealth through AE. This can be clearly evidenced through the difference in contribution rates – DB has an average contribution of 25.6% (19.2% employer/6.4% employee) with DC significantly lower with an average of 5.1% (2.4% employer/2.7%employee).

What factors relating to intergenerational fairness should be considered when determining the State Pension age?

Factors include existing SPA and the level of benefit paid, changes in national average life expectancy, likely outcomes delivered through AE, the annual indexation mechanism in place and the political commitments made to maintaining it, public expectations and whether the final proposals are sustainable for a defined period.

From a workplace pension perspective, we have moved away from retirement being defined by a single date with DB to typically, a flexible phased retirement approach with DC. We believe a small amount of the flexibility associated with modern pension systems should be integrated into the SP. It is currently possible to defer taking SP benefits to secure a greater level of future benefit - either through election or as a default in the event of a claim not being made. Given that personal circumstances come in all shapes and sizes, it would be appropriate to consult on a national approach, enabling limited early access flexibility. Although this option could be simply communicated, many will not be equipped to make such a decision and as such, we believe anyone wishing to claim early should evidence they have received regulated advice or attend a mandated MaPS guidance session.

One of the public criticisms that pensions have is they are too complicated. Any changes we make to the SP needs to adhere to the principles of simplicity and sustainability. There have been calls to base SP benefits on geographical location i.e. postcode. The complexity involved in creating, maintaining, communicating an understanding such a system would be huge. Immediate challenges which spring to mind which are by no means exhaustive are:

- Is entitlement based on number of years lived at a postcode, or where you have lived for most of your life or where you live at the point of claim?
- Is there partial eligibility? If yes, how is entitlement calculated and explained to the individual
- Eligibility rules could result in individuals gaming the system to qualify
- It creates an incredibly complicated system which would increase governance costs and makes retirement planning even harder for individuals

Aside from the operational issues above, there are several socioeconomic factors in play which impact life expectancy, with location being just one. To include all relevant elements realistically makes this impossible to achieve or understand. This further supports our proposal for a SP framework which provides everyone with the same potential entitlement to flexibility.

Is it reasonable to give people a fixed period of notice for State Pension age changes, and if so what period?

It would be unreasonable not to provide adequate notice. Given the significant impact the SP has on retirement outcomes then this should not be for a period of less than 10 years.
We have already provided above some of the long-term factors which need to be considered when setting a future SPA. However, we cannot predict the future with any certainty. In the interests of sustainability, the framework needs to have a degree of flexibility to make some interim smaller changes to reflect scenarios where assumptions are not borne out by events.

Our proposal is for individuals to be notified of their SPA prior to reaching Normal Minimum Pension age (NMPA - currently 55 rising to 57 in 2028) – the age calculation would be undertaken on an agreed periodic basis. All individuals receiving a communication at that time would be subject to the same SPA and this calculation would be based on an agreed actuarially based calculation process which reflects the principles of fairness and sustainability. Importantly, an individual SPA would not increase. The timing of this advance notice enables individuals to consider the use of private pension provision in the interim and would broadly provide a 10-year notification window.

Whilst the age should not increase from what has been communicated, the changing environment may differ from assumptions used and may mean that future indexation increases to pensions in payment will need to change to reflect existing market conditions, again based on the two principles of fairness and sustainability. We propose indexation should be reviewed triennially, rather than the use of a mechanism which creates an expectation based on unknown future variables, which may or may not be sustainable.

3.2. Changes in the nature of work:

How have changes to the types of jobs people do affected working lives?

The reopening of the economy post pandemic has seen the Service sector see the fastest growth in quarter of a century, however this is one of the lower paid sectors. Given that minimum contributions into an AE workplace scheme are unlikely to achieve good retirement outcomes even in conjunction with the SP, many employees and households may be forced to decide whether to extend their working lives or accept a lower standard of living and retiring at their originally selected age.

There are circa 4.2 million self-employed currently who accrue SP entitlement through a combination of Class 2, 3 and 4 NI contributions. Whilst a proposal to simplify the NI framework for this group and abolish Class 2 was ultimately removed, we believe this call for evidence provides an opportunity for a further review.

Whilst good retirement outcomes are dependent on more than state and private pension entitlement in isolation, pension wealth for the employed makes up a significant part of overall wealth, even eclipsing property wealth overall. There is currently no equivalent of AE for Self- Employed or the added incentive of an employer contribution, although we are aware a DWP working group is considering potential ways to bring more of this cohort into retirement saving. We look forward to seeing the outputs of this work given the low percentage of this group who actively contribute to private pensions.

The gig economy has risen in recent years with 1 in 6 adults working in this sector at least once a week. Despite the Uber ruling, there remains uncertainty over the employment status of most gig workers, which means many will not benefit from AE. This is also true for many part-time workers and multi-jobbers who earn under the earnings trigger in a single employment – this is an area which needs further review.

We also need to consider unpaid workers. An impact of an ageing population is a significant rise in the number of unpaid carers. 2019 statistics showed there were 5 million unpaid carers with an additional 2 million taking on responsibilities every year. 600 leave paid work on a daily basis due to these additional responsibilities, majority of which are women. This has an obvious impact on the ability to accrue retirement savings.

What are the anticipated future changes to the workplace? How could this impact on people's working lives?

The 2014 government publication 'The Future of Work Jobs and Skills in 2030' states it is not possible to predict the future. Previous predictions in the mid-90s of radically reduced working hours and increased leisure time by mid-2010s did not occur for instance.

We have seen a change to more flexible working practices due to the pandemic and we would expect an element of this flexibility to be retained on an ongoing basis.

Technology continues to play a large part in enabling flexible working practices to be adopted and can also help older workers remain in more physical employment.

Government initiatives and objectives are encouraging people to work for longer and there are options available to help develop new skills which can lead to extending working lives with a change of direction.

Pension freedoms have also enabled individuals to approach retirement on a phased basis and scale down the working hours over a period of time whilst supplementing lost earnings through private pension access.

Despite a trend of working for longer, Generation Z and Millennials typically expect to retire before 60. This is optimistic given the challenges that they face, however it is important that these expectations are considered in the planning of UK Pension systems and illustrates the importance of clear and unambiguous communications.

As mentioned above, we would also expect the number of unpaid carers to continue to increase with a corresponding number leaving the workforce early to meet these commitments.

What factors do people consider when making decisions about when to retire?

Despite these being decisions based on a variety of personal circumstances, typical factors include the ability to continue to work, total wealth, caring responsibilities, health, availability of retraining initiatives and retirement expectations. Most will not be equipped to make these decisions on an informed basis without seeking regulated advice or guidance.

We would reiterate that due to the shift of workplace pension provision to DC, retirement decisions are no longer the cliff-edge they once were and many will approach retirement on a phased basis, often taking several years or more to fully transition.

3.3. Sustainability and affordability:

What is the most sustainable and affordable way of managing the cost of State Pension in the longer term? What are the advantages and disadvantages of potential options?

As mentioned above, the SP needs to meet a to be determined 'fairness' measure which is based on the economic and demographic environment, both current and expected and periodically reviewed. Whilst fairness needs to be consistent, the actual benefits will be relevant to the factors in play, unless there is a political desire to increase expenditure and raise tax revenue or allocate money from elsewhere.

We need to recognise that some elements, such as future increases, cannot be guaranteed for an indefinite period of time due to the uncertainty of what the future holds. Creating such an expectation aside from being unsustainable, is misleading and risks retirement planning being made on incorrect assumptions.

A framework with agreed periodic reviews conducted within a controlled governance framework is required to provide sustainability. The pay as you go system does not perform well for ageing populations and the creation of a ringfenced SP fund should be explored to provide more certainty and act as a buffer for future generations.

Our proposal is for individuals to be notified of their SPA prior to reaching NMPA (currently 55 rising to 57 in 2028) - the age calculation would be undertaken on an agreed periodic basis. All individuals receiving a communication at that time would be subject to the same SP and this calculation would be based on an agreed process which reflects the principles of fairness and sustainability. Importantly, an individual SPA would not increase. The timing of this advance notice enables individuals to consider the use of private pension provision in the interim and would currently broadly provide a 10-year notification window.

Whilst the age will not increase from what has been communicated, the changing environment may mean that future indexation increases will need to change to reflect existing conditions, again based on the two principles of fairness and sustainability. We propose these should be reviewed triennially, rather than the use of a mechanism which creates an expectation based on unknown future variables, which may or may not be sustainable.

3.4. Metrics for setting State Pension age

Is it reasonable for people to expect to spend a fixed proportion of their adult life in receipt of State Pension?

It is reasonable for people to expect to be treated in a fair and consistent manner, relevant to the current and expected financial and demographic environment. Unless there is significant and catastrophic change, this should result in people of all generations receiving SP benefits for broadly similar time periods based on average national life expectancy.

Are there options for taking account of differences in circumstances when setting State Pension age in future? What are the advantages and disadvantages of these options, and how could they operate within the current pensions framework?

One of the public criticisms that pensions have is they are too complicated. Any changes we make to the SP needs to adhere to the principles of simplicity and sustainability. There have been calls to base SP benefits on geographical location i.e. postcode. The complexity involved in creating, maintaining, communicating an understanding such a system would be huge. Immediate challenges which spring to mind which are by no means exhaustive are:

- Is entitlement based on number of years lived at a postcode, or where you have lived for most of your life or where you live at the point of claim?
- Is there partial eligibility? If yes, how is entitlement calculated and explained to the individual
- Eligibility rules could result in individuals gaming the system to qualify
- It creates an incredibly complicated system which would increase governance costs and makes retirement planning even harder for individuals

Aside from the operational issues above, there are several socioeconomic factors in play which impact life expectancy, with location being just one. To include all relevant elements realistically makes this impossible to achieve or understand. This further supports our proposal for a SP framework which provides everyone with the same potential entitlement to flexibility.

How can we best take into account the sensitivity of the life expectancy projections when considering an appropriate State Pension age for the future?

Our proposal creates periodic reviews for people approaching NMPA based on actuarially based calculations to provide their SPA which will commence in X years' time. This would broadly be 10 years based on current factors, however future changes may impact on that timeline – the important aspect here is the date/age provided will not increase once it is communicated. Where assumptions used to determine the communicated SPA such as life expectancy significantly change, it may be necessary to adjust the level of future indexation increases once SP is in payment.

Are there other metrics which are relevant or more suitable to help determine State Pension age in future, and if so, what metrics?

A recurring theme in this response articulates that the SPA needs to be determined by a variety of factors which includes national average life expectancy and the current and expected economic and demographic environment (number of workers vs pensioners). This needs to be calculated on a regular basis for those approaching NMPA.

The measures of success need to be measured through meeting defined fairness and sustainability standards.

What factors do other countries consider when determining State Pension age?

All countries face the same challenges in this regard. Pension systems and other state benefits do vary, often considerably across OECD countries and whilst the challenges and components remain broadly consistent, the approach and weighting applied to these will differ. It needs to be recognised it will not be possible to perform comparison exercises on a 'like for like' basis.

3.5. Additional information

Do you have any other comments which relate to the Terms of Reference of this review, that you wish to share?

When reviewing the SP, we need to also consider other national pension systems that are in place. It is common among OECD countries for total pension provision to be made up of several components or pillars, with different funders, benefits, retirement ages and contribution structures in place for each.

For UK, the other pension system we have in place is Auto Enrolment (AE). As participation amongst eligible employees has exceeded 85%, this is now considered by OECD as a quasi-mandatory scheme. We should ensure that all reviews and changes to the SP take in to account the overall retirement income targets that are deemed appropriate and the impact this has on AE's ability to deliver on the income level that will be required from a private pension.