

# United Kingdom

## Introduction – a note on the effectiveness of pensions information in the UK

The UK's Pension Reforms (see our response to Question 1) – in particular, the use of automatic-enrolment - are based largely on evidence that **information alone will not be enough to solve the under-saving problem**. Much of this was concluded as a result of the Department for Work and Pension's (DWP's) Informed Choice Programme (which ran between 2004 and 2006) and its associated programme of research and evaluation.

The initial conclusion from Informed Choice was that *'Information on its own is unlikely to result in many people taking out a pension or increasing their contributions, but it does have a valuable contributory role as lack of understanding clearly underpins a number of the barriers'*<sup>1</sup>.

The evidence indicated that although information is valued by many who read it, large numbers of people do not engage with it. Pensions are seen as complex products, many lack the necessary level of financial capability and it is easier to put off making any provision due to the long time horizons involved.

Also, more recently, The Pensions Commission<sup>2</sup> thought there was *'limited impact of providing better information and generic advice'*. The 2006 White Paper<sup>3</sup> agreed that *'information and significant financial incentives are often insufficient'* to address inertia and low levels of understanding of pensions.

It should be noted, however, that most initiatives within Informed Choice only had a few years to be developed and were delivered in a more uncertain pensions environment than should exist post-reform, so the findings can inform but cannot be transposed directly to the future environment.

Therefore, in the 2006 White Paper (see footnote 3), and debates during the passage of the Pensions Bill currently before Parliament, we have acknowledged that **providing people with good information will be a crucial aspect of the reforms**.

Consequently, work is underway in DWP, to develop a long-term Pensions Reform Communications Strategy which aims *'To help people to take personal responsibility for their retirement planning and contribute to enabling them to make appropriate choices about working longer, planning and saving for retirement'* (see our response to Question 1.1 for more information).

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<sup>1</sup> Green, E and White, C (2005), Effective means of conveying messages about pensions and saving for retirement; DWP Research Report 239.

<sup>2</sup> 'The second report of the Pensions Commission' (2005).

<sup>3</sup> 'Security in retirement: towards a new pension system' (2006).

At the same time, the UK Government has launched its long term approach to financial capability (see our response to Question 2.4) and a major review of *generic financial advice*<sup>4</sup> (which includes that provided for pensions and pensions planning) in the UK. The review of generic financial advice<sup>5</sup> undertaken by Otto Thoresen, has concluded that that a national service of *Money Guidance* (Thoresen's description for financial information and generic financial advice) is both wanted, needed and beneficial for the UK population, the financial services industry, the Government and society as a whole. The Review recommends that the Money Guidance service can be fully implemented as soon as possible, and that a *Pathfinder* should be in place as soon as possible in 2008.

## 1. Session one: Informing on change

### 1.1 What do individuals know about main aspects of the pension systems that are changing? (parameters, financing, retirement age, indexation)

#### Background to UK pension system changes

The UK has recently undertaken a fundamental review of its pensions system to consider what is required to deliver a sustainable pension system in the short and long term. This is referred to in our responses as our *Pensions Reforms*.

The Pensions Act 2007, which became law on 26 July 2007, made changes to the State Pension system in the UK. These changes include:

- introducing of a new system of credits which will increase the number of people who would become entitled to a State Pension
- increasing the basic State Pension by the increase in the rate of average earnings – this will happen by the end of the next Parliament at the latest
- increasing the State Pension age from 65 to 68 between 2024 and 2046, and
- stopping people from 'contracting out' of the additional State Pension when they are in defined-contribution occupational pension schemes and personal pension schemes.

The Government also plans to bring in more laws (the current Pensions Bill is currently going through Parliament) to introduce a new low-cost saving scheme (called personal accounts) and an employer obligation to automatically enrol eligible employees into a suitable pension scheme or personal accounts, as well as more measures to improve the State Second Pension, from 2012.<sup>6</sup>

<sup>4</sup> See our response to question 1.3 for further information.

<sup>5</sup> Thoresen Review of generic financial advice. For full details see: [http://www.hm-treasury.gov.uk/media/8/3/thoresenreview\\_final.pdf](http://www.hm-treasury.gov.uk/media/8/3/thoresenreview_final.pdf)

<sup>6</sup> For more information, see <http://www.thepensionsservice.gov.uk/pensionsreform/personal-accounts.asp>

## Evidence from research

Qualitative<sup>7</sup> research<sup>8</sup> was carried out in 2005 to look at general knowledge and attitudes towards pensions and responses to suggestions for change in the pension regime in advance of the publication of the second report of the Pensions Commission that was published at the end of November 2005. The study was intended to help inform the Department for Work and Pensions (DWP) response to this report and develop the pension reforms included in the Pensions Act 2007 and the current Pensions Bill.

The main findings were:

- General understanding about the extent of state pension provision and the way in which it is calculated was poor. Individuals often assumed that the state pension is paid at a higher level, that there is universal entitlement to the state pension or that all those entitled receive the same level of award.
- Widespread media attention had alerted most individuals to the fact that there is some form of 'problem' with the pension system. However, the reasons behind this were very difficult for most individuals to grasp. This was because individuals were largely unaware of (the extent of) the increase in average life expectancy that has taken place since the introduction of the state pension and also because there was limited understanding of the way in which the system operates.
- In general, people felt that the balance of responsibility for funding retirement lies with the individual and the Government (but only in as far as providing a safety net to ensure people were not living in poverty). Employers were seen to play a much smaller role, being primarily viewed as a facilitator, although employers were the main route through which those who had a pension had obtained it.
- In discussion of automatic enrolment in a private pension scheme, people were supportive of having an employer contribution.
- Responses to raising the state pension age were highly emotional and it was viewed as synonymous with forcing individuals to work longer (even by those who stated that the state pension age would have no bearing on when they elected to retire).
- However, there was some grudging acceptance that a change of this nature was inevitable among younger participants (who felt the state pension may well be phased out entirely by the time that they come to retire).
- Reactions to the suggestion of compulsory saving for retirement were mixed. Some viewed this as a potentially positive development encouraging people to start saving earlier, whilst others reacted negatively to the removal of individual choice stating that they should be allowed to choose alternative ('better') mechanisms for retirement saving

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<sup>7</sup> Qualitative research serves primarily to identify and explore views about the subject, but not the extent to which these are held. As such, these findings should be treated as indicative only.

<sup>8</sup> Department for Work and Pensions Research Report No 357: "Pensions and pension reform". For details of the methodology for this research and a fuller summary of the key findings, see <http://www.dwp.gov.uk/asd/asd5/rports2005-2006/rrep357.pdf>

or to be able to prioritise other areas of expenditure (generally younger individuals looking to start on the property ladder or to pay off student debts).

- Although most did not view the facilitation of retirement saving as an employer responsibility, automatic enrolment in employer schemes was generally viewed as a positive suggestion.
- Most acknowledged that compulsory employer contributions would make automatic enrolment a more attractive prospect. It was clear that employer contributions had played a role in encouraging most of those who were members of their employer scheme to join.
- Widespread distrust of employer and private pensions (fuelled by media coverage of 'horror stories') led individuals to raise concerns over being 'forced' to use unreliable savings mechanisms if either compulsion or automatic enrolment were to be introduced.
- The majority of individuals were uncomfortable with the concept of 'risk' in the context of pensions. They felt that it was inappropriate to take risks with such an important investment.

To inform the Government's subsequent 2006 White Paper<sup>9</sup>, the UK also conducted the National Pensions Debate to gather the views of thousands of people through public events, an online Debate and via stakeholder events. The findings of the Debate were published May 2006<sup>10</sup> and echo many of the views held by people in the above mentioned research report. The main messages from the Debate were:

- People agreed overall with proposals to increase working life but many people simply felt resigned to working for longer rather than positively choosing it.
- People favoured a State Pension system in which people are rewarded for contributing something to society.
- People thought a variety of non-work activities should count as contributions to the additional State Pension
- The majority considered the proposed introduction of the employer obligation to automatically enrol eligible employees into a suitable pension scheme or the personal accounts scheme to be a useful way of encouraging more people to save more for their retirement.

More recently, DWP conducted qualitative research<sup>11</sup> into younger people's (aged 16 to 29) attitudes to saving and pensions reforms.

The report concluded that young people face a variety of barriers to saving for their retirement, including a strong sense of wanting to 'live for today', competing demands on their income and a poor understanding of the available pension options.

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<sup>9</sup> 'Security in retirement: towards a new pension system'.

<sup>10</sup> Department for Work and Pensions National Pensions Debate Final Report May 2006. For the full findings from the National Pensions Debate, see [http://www.dwp.gov.uk/pensionsreform/debate/final\\_report.pdf](http://www.dwp.gov.uk/pensionsreform/debate/final_report.pdf)

<sup>11</sup> Department for Work and Pensions, Research Report No 438: Live now, save later? Young people, saving and pensions (2007). For the full report see: <http://www.dwp.gov.uk/asd/asd5/rports2007-2008/rrep438.pdf>

Against this general background of apathy towards pension saving, it was encouraging that automatic enrolment and personal accounts were mostly very well-received by participants. This research found that personal accounts may even act to improve understanding of the need to save for pensions more generally, and the benefits of employer pensions in particular. However, the research concluded that many young people will need persuading that they need to start saving *before* the scheme is introduced in 2012.

DWP has conducted a survey<sup>12</sup> of individuals who would be eligible for automatic enrolment under the Government's reforms about their attitudes and likely reactions to the reforms and to the personal accounts scheme. This survey included questions about people's awareness of the scheme, and the sources they would most like to receive information about it from. Some key, top-line findings from the survey are published in a Fact Sheet (this is attached for interest at **Annex A**), however, the findings which are of most relevance to this questionnaire are currently unpublished. Publication of the report containing full findings and analysis from the survey is anticipated this summer.

### Pensions Reform communications

The UK Government, through DWP, is ensuring that all information requested by individuals – via contact centres, leaflets or websites, for example - is accurate and up-to-date in the light of the Pensions Act 2007. Also, as part of the Pensions Reforms, customer information leaflets have been comprehensively reviewed and rationalised to ensure clarity, accuracy and consistency of information provision. Pre-publication, each leaflet underwent customer testing to ensure the quality of information provision met required standards. To help improve understanding of often complex subject matter, all leaflets are now clarity approved by the Plain English Campaign. A central online information database is also being developed to maintain accurate and consistent information provision across all customer communication channels.

To help people plan for retirement, DWP continues to provide access to pensions information services such as: personalised pension forecasts; a pension tracing service; state pension deferral information; generic information (through a suite of letters, forms, leaflets and downloadable online documents); and pensions guidance via the Pensions Advisory Service. A new leaflet, 'Pensions: the basics', was launched in September 2006. It provides people with accessible information about pensions options and explains the benefits of saving into a pension.

DWP also uses a range of cross-media campaigns to build and maintain awareness relating to pensions planning and entitlement. These sign-post customers to a range of further sources of information; e.g. Pensions Centres, Pensions Information Line. Currently, DWP is proactively raising awareness of changes such as State Pension Age (SPA) equalisation among affected women, and helping carers understand how Pensions Reform might affect their entitlements, for example, through some short term communications activity including a direct mailshot to 1.7m women on State Pension age equalisation, advertorials and Public Relations activity. Earlier research<sup>13</sup> conducted by DWP in 2004, showed that 59 per cent of all working-age (between the

<sup>12</sup> Forthcoming in 2008 : Individuals' attitudes and likely reactions to the personal account reforms 2007: Report of a quantitative survey.

<sup>13</sup> DWP Public awareness of State Pension Age equalisation Research Report No. 221. For full details see: <http://www.dwp.gov.uk/asd/asd5/rports2003-2004/rport221/Main.pdf>

ages of 16 and SPA (60/65)) survey respondents, said they were aware of the future increase in women's SPA.

The 2006 Attitudes to Pensions survey<sup>14</sup> included a knowledge test to assess whether respondents perceived knowledge of pensions matched their actual knowledge. This found that there were high levels of awareness that the age at which women can receive their State Pension will increase in the future. Women were generally more aware than men.

DWP is also currently in the process of developing a new, longer-term communication and information strategy informed by a continually enhanced evidence base, which will enable and encourage more people to plan and save for their retirement (including the option of remaining in employment for longer). This new strategy will ensure that individuals are equipped with the necessary facts and understanding so that they are able to make the necessary decisions about their retirement planning. The target group for this strategy is likely to include those being auto-enrolled, those who are otherwise in danger of retiring without sufficient means and those seeking information to support their retirement planning.

The strategy is intended to support the Pensions Reform agenda outlined in the May 2006 White Paper. Many of the reforms announced in the White Paper will not begin to be implemented until 2012, and the strategy will cover our communications objectives for the period from now until their implementation is complete. As part of the strategy, we are developing a comprehensive approach to measuring and evaluating its success. Some of the key objectives of the strategy are around supporting the introduction of automatic enrolment, and the ultimate success of this agenda and the supporting communications activity cannot be known for a number of years. But the evaluation of the strategy overall will be an ongoing process, with regular internal reporting.

Evidence-based information will also be developed to ensure the smooth introduction of personal accounts and reforms around automatic enrolment from 2012. By ensuring adequate information is available in a simple and clear form, individuals will be able to make their own choices in relation to these reforms. Government will work with stakeholders, including The Personal Accounts Delivery Authority, to ensure that the information available is both coherent and consistent.

### Enhancing our evidence base – further research

The UK Government is also continuing to enhance the evidence base by commissioning research to improve understanding of individuals' information needs and behaviour in response to information about pensions and retirement planning.

Equally, lessons will be learned about how information and guidance can best be delivered from initiatives aimed at increasing people's awareness of the need to, and value of, planning ahead for retirement such as the '50+ Face to Face Guidance Pilot Project and the Pensions Education Fund (PEF). (See **Annex B** for a brief explanation of PEF). Research findings from the 50+ Face to Face Guidance Project pilots, that are due to end March 2009, will inform the development of best practice for Government and non-government organisations to use in the guidance that they

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<sup>14</sup> Department for Work and Pensions Research Report No 434: "Attitudes to pensions: The 2006 survey". For details of the methodology for this research and a fuller summary of the key findings, see <http://www.dwp.gov.uk/asd/asd5/rports2007-2008/rrep434.pdf>

offer older workers. A DWP report on the evaluation on Pensions Education Fund (PEF) will be published in spring 2008.

## 1.2 What do individuals know of the different types of financial risks to which individuals are exposed and on which they can make choices (longevity, rates of returns guarantees...)?

Qualitative research<sup>15</sup> carried out in 2006 to look at general knowledge and attitudes towards pensions and responses to suggestions for change in the pension regime showed that the majority of individuals were uncomfortable with the concept of 'risk' in the context of pensions. They felt that it was inappropriate to take risks with such an important investment. Many were unaware that pension funds are invested on the stock market and tended to view them as long-term savings accounts instead. Most stated that, if they were given the choice, they would select low risk funds (despite the fact that these would be likely to have low rates of return). Nearly all felt that they were not equipped to make this sort of decision and that they would prefer to leave these sorts of decisions to an 'independent financial adviser' or pension provider.

Furthermore, the 2006 attitudes to pensions survey<sup>16</sup> found that 71 per cent of individuals agreed that it was better to play safe than to take risks with their savings. More than two-thirds (69 per cent) would prefer a medium-risk pension fund, compared to one with a low or high risk and 64 per cent believed that a pension fund linked to the stock market was too much of a risk. Around a third (34 per cent) of individuals felt they had a clear idea what to do when making important financial decisions. Men and older respondents were more likely to state this.

One of the topics of interest covered in research carried out by the Financial Services Authority in 2005 and published in 2006,<sup>17</sup> was peoples' preference for risk with investments. The survey found that 43 per cent of respondents did not want to take any risk with their savings. In fact, a significant proportion of respondents owned products with an element of risk to their capital, yet their preference was to have no risk exposure at all. (See also our response to Question 2.3 for more information about this research on financial knowledge and capability). More detailed but earlier findings on people's understanding of financial risk, can also be found in the Financial Services Authority's research report on consumer understanding of financial risk.<sup>18</sup>

It may also be of interest to note that DWP has recently conducted an in-depth qualitative study exploring individuals' understanding of and preferences for investment fund choice (and consequently financial risk) within the context of personal accounts. The results from this survey are currently unpublished, but publication is anticipated for summer/autumn 2008.

Research from Which? in 2004, found that consumers in focus groups were generally negative about pensions. They saw pensions as inflexible, distrusted them as a savings mechanism and their perception was that the process of acquiring a pension could be complicated. They also viewed property as a less risky way to save.

<sup>15</sup> DWP Research Report No 357: "Pensions and pension reform". For details of the methodology for this research and a fuller summary of the key findings, see <http://www.dwp.gov.uk/asd/asd5/rports2005-2006/rrep357.pdf>

<sup>16</sup> Attitudes to pensions: the 2006 survey by Clery et al. DWP research report number 434. Published in 2007.

<sup>17</sup> Consumer Research 47 Financial Services Authority, "Levels of Financial Capability in the UK :Results of a baseline survey". See <http://www.fsa.gov.uk/pubs/consumer-research/crpr47.pdf> for the full survey.

<sup>18</sup> Consumer Research 33 Financial Services Authority: Consumer understanding of financial risk. See <http://www.fsa.gov.uk/pubs/consumer-research/CRPR33.pdf>



The focus groups saw the ideal pension being characterised as:

- guaranteed and risk free
- flexible (portable)
- independent and not for profit
- easy (no effort to acquire or operate)
- transparent and simple (no small print).

Which? also carried out quantitative research in February 2006 looking towards a new national pensions savings vehicle. Consumers (60%) were looking for security and low risk rather than a higher rate of return. This echoed the research from October 2004, where 64% preferred a lower rate of return but a higher degree of certainty.

Seeing financial services in the round, trust is the key issue and financial services companies do not rate high on trust indices. In a Harris survey in 2006, 9 out of 10 rated trust as the most important factor for financial services - above customer care and innovation.

Which? concludes that that to create confidence in pensions consumers need:

- increased skills which empower them and therefore generate action
- choices made easier with simplified information
- help provided when needed in an appropriate way
- trust in an advice brand
- a credible pension offer
- flexibility in the pension offering.

### 1.3 How are people informed about these questions and how can the efficiency of this information be assessed? What are the main tools to provide information to individuals?

In his recent Review<sup>19</sup> to identify and recommend the best model for delivering financial information and generic financial advice services in the UK, Otto Thoresen looked at how people are informed about different financial products.

Whilst not isolating how people are informed about risk itself in relation to these products, Thoresen highlighted that different providers meet different information and advice needs as follows:

- product providers provide help and guidance about their products,
- regulated advisers<sup>20</sup> usually provide their clients with help and ongoing advice, and

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<sup>19</sup> Thoresen Review of generic financial advice. For full details see:  
[http://www.hm-treasury.gov.uk/media/8/3/thoresenreview\\_final.pdf](http://www.hm-treasury.gov.uk/media/8/3/thoresenreview_final.pdf)

<sup>20</sup> Whilst there is therefore no formal definition in the UK of the term regulated financial advice, it is often used to mean advice provided through Independent Financial Advisers (IFAs) or through personal advisers in Banks and Building Societies. It is advice given by professional advisers as part of activities regulated by the Financial Services Authority in assessing an individual's personal circumstances, and usually includes product recommendations and sale. By contrast, generic financial advice takes account of an individual's personal financial circumstances, but does not recommend particular products.

- specific services cover particular areas; for instance, The Pensions Advisory Service (TPAS) offers a service where pension savers can have questions answered, problems addressed and disputes resolved.

However, Thoresen also noted that research shows people to be generally poor at choosing products (he quoted that 46 per cent of people surveyed by the Financial Service Authority did not collect any information on products before making a decision).

In earlier research<sup>21</sup>, the FSA identified and assessed the effectiveness of different channels or ways of providing information about financial risk.

The research found that:

- The likelihood of considering investments is strongly influenced by the media, marketing activity and personal recommendations. These are channels that potentially may be used more effectively to communicate the issue of risk, but unfortunately, it is also via these channels that product misperceptions can be formed if these information sources are only referenced on a sporadic basis and considered in isolation. It can result in consumers failing to see the complete picture, especially when the press overemphasise the negative, yet rarely promote the positive.
- Interest in the internet as a channel for financial information was mainly confined to respondents who were young and/or of medium to high financial sophistication. Face-to-face interaction was the preferred approach amongst the less sophisticated.
- Many respondents acquired information concerning investment risk in a passive manner. Typically, it was only respondents of medium or high financial sophistication that actively sought information regarding risk, but this mainly concerned the risk-to-return ratio as opposed to different types of investment risk.
- Some respondents claimed to be very happy with the financial advice given concerning their investment product and its relative risk, even though they may not have understood how their product works or be able to remember discussions about risk. Others felt investment risk should have been given greater prominence in the sales process, as it was either not discussed or was marginalised.

The research also went further to assess the effectiveness of discussions about risk with financial advisors. It found that:

- There was generally a poor recollection by consumers of discussions about risk with financial advisers. Some respondents believed the matter of risk was never raised and often had no recollection of the discussion of alternative product options with their advisor either.
- Other respondents believed the issue must have been mentioned for them to feel the right decision had been made, but they could not recall the exact content of the discussion.

<sup>21</sup> Financial Services Authority Consumer research 33: Consumer understanding of financial risk November 2004. See: <http://www.fsa.gov.uk/pubs/consumer-research/CRPR33.pdf>

- Financial advisors in the sample however, said that there was a very strong emphasis on explaining risk and it was raised through a number of stages of the advice process ie from the initial fact find exercise and the report issued by the adviser following the consumer consultation which summarised the discussion held and the reasons for product recommendations through to the statutory warnings and the “key features” document.
- However, advisors acknowledged that many customers switched off, passed the responsibility to partners or did not read the literature. Despite attempts by financial advisors to inform consumers about risk, they admitted that many consumers did not fully understand the information and they were happy to pass responsibility to the adviser if trust had been established.

See **Annex C** for an account of tools and services used (as at 22<sup>nd</sup> June 2007) to provide information about pensions and pensions planning to people in the UK.

## 2. Session two: Informing on choices

### 2.1 What are the actual main choices available to individuals (including portfolio profiles, etc...)? What are the choices of financial products individuals have: in the mandatory system (i.e. opt-out to the employers’ scheme), in the second and third pillars?

#### State Pension – the first pillar

The current rules for building up UK State Pension are based on the principles of the system introduced around 60 years ago by the 1948 National Insurance Act. State Pension is “earned” over a working life from age 16 to State Pension age. Women’s State Pension age is currently 60 and men’s State Pension age 65. Women therefore earn a State Pension over a working life of 44 years and men a State Pension over a working life of 49 years. However the State Pension age for women is going to rise to 65. This will happen between 2010 and 2020 and from 6 April 2020, the State Pension age for all women will be the same as it is for men. From 2024, the State Pension age for both men and women will increase by one year in every decade to reach 68 in 2046. This change will affect anyone born on or after 6 April 1959.

UK State Pension can only be paid if a person has reached State Pension age and a claim is made. It is made up of two elements basic State Pension and additional State Pension (the latter is also known as the State Second Pension).

To qualify for any basic State Pension a person has to satisfy two National Insurance contribution conditions. The amount of basic State Pension payable, if any, depends on the number of National Insurance qualifying years a person has. To receive a full basic State Pension a person normally needs to have qualifying years for around 90 per cent of their working life.

Married women who do not have enough qualifying years to receive a basic State Pension in their own right can derive a pension from their husband’s contribution records.

The basic State Pension is supplemented by an earnings related component, the additional State Pension, also known as the State Second Pension (S2P). Reforms to the state scheme in 2002 have focused extra help on people with low and moderate earnings, who cannot make significant private provision for their retirement. Additionally, it makes provision for certain carers and disabled persons. Individuals can choose to contract out of the State Second Pension (S2P) and accrue a supplementary pension in either an occupational or personal pension scheme. In return for contracting out and to offset the cost of providing the pension both the employer and employee in a defined benefit scheme pay a reduced rate of National Insurance Contributions (NICs) - this is known as the 'contracted-out rebate'. When contracting out is through a personal pension both employer and employee pay the full national insurance contributions but receive a rebate from the government. Increasing numbers of people qualify for a State Second Pension. Currently 23 million people are covered by the scheme and changes introduced from 2010 will extend coverage to a further 1 million people.

The government's first priority is to help those in greatest need, whilst rewarding those who have made savings for their retirement. Pension Credit (whilst not strictly a choice, but included here to complete the picture about the State Pension system) is an income-related benefit and it is tapered to reward those with private income and provides for generous disregards of capital. Pension Credit also acts as a gateway for a number of other benefits such as help with housing and local taxation costs (council tax).

In 2010, the basic State Pension is expected to be worth £87 in current earnings terms. This is equivalent to 19% of the average wage. In addition to this, assuming that the individual has been contributing since age 25, s/he should qualify for £88 in State Second Pension in current earnings terms, and £11 in income-related benefits. Summing up all these benefits, those with a full contribution record can look forward to benefits equivalent to just under 40% of the average wage in 2010.

Also, the UK Government is introducing changes to the uprating of basic State Pension so that during the next Parliament, the link between basic State Pension and average earnings will be reinstated. As a result, someone retiring in 2050 with a full contribution record and who is opted in to the personal accounts scheme, can look forward to having an overall replacement rate of close to half the average wage.

#### Private pensions – the second and third pillars

Supplementary pension provision is an important element of the UK pension system. The bulk of saving is through occupational pension schemes, which are voluntary for both the employer and the employee. Personal pensions offer an additional way to save for retirement. The introduction of stakeholder pensions, a form of personal pension with low charges, has encouraged a higher take up of such savings vehicles.

Occupational pension schemes may be established on either a defined benefit (salary related) basis or a defined contribution (money purchase) basis, specified in the scheme's governing documentation. Personal pension schemes are always set up on a defined contribution basis.

## Defined Benefit (Salary Related) Schemes

Defined benefit schemes usually calculate pensions on the basis of a specified fraction, e.g. 1/60 or 1/80 or 1/120, of the member's final or average salary for each year of service. There is no limit on the amount that can be contributed to a registered pension scheme for UK residents aged Under 75. Tax rule changes made in 2006, introduced a standard lifetime allowance, set at £1.6m for the 2007/08 tax year. However, tax relief is limited to relief on contributions up to the higher of 100 per cent of UK taxable earnings and £3,600. Employer contributions to these schemes are based on a specified percentage of the member's earnings, or a cash amount, and can also be dependent on members' contributions (matching arrangements) and/or age and length of service.

## Defined Contribution (Money Purchase) Schemes

Defined contribution schemes do not specify in advance the level of pension payable. Contributions to these schemes are based on a specified percentage of the member's earnings, or a cash amount, and can also be dependent on members' contributions (matching arrangements) and/or age and length of service. These contributions and the investments that accrue from their investment are used either to pay a pension or purchase an annuity on retirement. These contributions and the investments that accrue from them are used to receive a pension on retirement. This can either be a pension from a scheme or from an annuity.

## Mixed Benefit Schemes and Hybrid Schemes

These schemes have both defined benefit and defined contribution elements. Some schemes provide a member with a pension, which is based on the better of the defined benefit pension or the defined contribution pension calculated by reference to that member's service and contributions. Some employers operate schemes comprising of two sections: one defined benefit and the other defined contribution. Scheme rules will say which employees can join each section and the circumstances in which members can move between sections.

## Personal Pensions

Personal pensions are pensions that individuals take out with financial services companies such as banks and insurance companies. Personal pensions are individual contracts and are not directly related to an individual's employment. An individual can change employers and still contribute to the same personal pension. An employer can contribute to his employees' personal pensions, all of which operate on a defined contribution basis, and which attract tax relief on contributions. All personal pensions operate on a defined contribution basis. Personal pension holders have to pay charges for the administration of their pension; the charges are set out in the contract.

A group personal pension (GPP) is an arrangement tailored for the needs of the employees of a particular employer. By potentially offering economies of scale, it may be more cost effective than individual pension arrangements. The actual personal pensions under the arrangement are personal pensions between the employees and the personal pension provider, although the employer may make contribution.

## Stakeholder Pensions

Stakeholder pension schemes are low-charge, flexible pensions for those who cannot join a suitable company pension scheme and for whom other types of personal pensions may be unsuitable. They are intended primarily for people on moderate earnings, although they are an option for others, including non earners who may be thinking about taking out a private pension.

Stakeholder pension schemes can be established by financial service organisations, representative organisations (such as trade unions or trade associations) and employers. Stakeholder pension schemes are required to limit management charges to a maximum of 1.5 per cent of the value of the individual's pension fund each year, for the first ten years, before continuing at a 1 per cent charge cap. They are allowed to offer 'with profits' investments, though any charges must be contained within the stipulated 1 per cent charge. They are also required to be flexible so that participants can vary contributions or move between schemes without being penalised.

## Annuitisation

At retirement the vast majority of people with a defined contribution pension use the fund that has built up during their working life to purchase an annuity. An annuity is a contract or agreement under which the individual receives fixed payments for their lifetime or for a specified number of years. The individual can purchase the annuity from the company with which they built up their pension fund, or with an alternative company. There are number of different types of annuity that can be bought, and the individual will need to consider which is the most appropriate given his or her individual circumstances. The main types of annuities are single life, where the payments stop when the individual dies; joint-life, where payments are made to a spouse or civil partner after the individual dies; level, where the income is a fixed amount; and escalating, where the payments are index linked.

## 2.2 What are the actual choices people take regarding their pensions (deferred pension, partial pension, different types of annuities, share of lump-sum...)?

### Choice about when to claim State Pension

People can draw their State Pension once they reach State Pension age (SPA), even if they continue working. Alternatively they can put off (defer) claiming, and earn extra weekly State Pension or, if they put off claiming for at least 12 consecutive months, they can claim a one-off taxable lump sum. Based on 2006 (the latest available) data, approximately 10 per cent<sup>22</sup> of those reaching SPA have deferred. The large majority of those deferring are women, due to the difference in SPA and lower entitlements. The typical period of deferral is 2-3 years, 2 years for men and 3 years for women.

The UK Government recognises that the decision about whether to put off claiming state pension is an important decision which may affect tax and other social security benefits, so recommends that people seek independent advice before making this decision. DWP undertakes to ensure people have access to *information* (it is not Government's role to provide financial advice ) that clearly sets out what options they have and how these options are affected by tax and other

<sup>22</sup> Only an estimate can be given because no "action" is required to defer a state pension and we only pick up "deferrers" when they go on to claim State Pension and become part of DWP administrative records.

benefits. Special rules were introduced into Pension Credit, Housing Benefit and Council Tax Benefit to help those who opt for the one –off lump sum payment of their deferral reward (ie the sum received is disregarded for life.)

### Claiming Pension credit

Data captured at May 2007 (our latest published administrative data) showed that 2.7 million pensioner households were claiming Pension Credit. We estimate (based on 2005/06 data<sup>23</sup>) that take-up for Pension Credit as a whole is currently between 60 and 69% per cent of those who are eligible. However, take up for *the Guaranteed Credit* element is estimated to be higher – between 70 to 81 per cent (based on the same data).

### Private pensions – choices people actually make

Data from the Office for National Statistics (ONS) Annual Survey of Hours and Earnings (ASHE) provides information on the percentage of employees who are members of employer-sponsored pension schemes by type of scheme in the UK:

#### Employee membership of an employer-sponsored<sup>1</sup> pension scheme: by pension type

United Kingdom	Millions					
	Defined benefit occupational	Defined contribution occupational	Group personal pension	Stakeholder pension	Pension type unknown	All provision
2005	8.9	1.7	1.4	0.8	0.7	13.4
2006	8.5	1.8	1.5	0.9	0.8	13.5
2007	8.4	1.6	1.6	0.9	0.7	13.5

1 Pension is arranged through an employer, main pension only.

2 Data for 2005 were based on a slightly different methodology than data in later years

Source: Annual Survey of Hours and Earnings, Office for National Statistics

Data from HM Revenue and Customs provides information on memberships of personal and stakeholder pensions in the UK:

#### Members of personal and stakeholder pensions (thousands)

	2002/03	2003/04	2004/05	2005/06	2006/07
<b>Personal pensions</b>					
Employer sponsored schemes	1,810	1,710	1,750	1,890	1,930
Non-employer sponsored schemes	7,740	7,110	6,690	6,330	6,120
<b>Total</b>	<b>9,550</b>	<b>8,820</b>	<b>8,440</b>	<b>8,220</b>	<b>8,050</b>
<b>Stakeholder pensions</b>					
Employer sponsored schemes	620	800	790	870	950

<sup>23</sup> Income Related Benefits Estimates of Take-Up in 2005-06, (2007) DWP.

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Non-employer sponsored schemes	640	670	720	810	850
<b>Total</b>	<b>1,260</b>	<b>1,470</b>	<b>1,510</b>	<b>1,680</b>	<b>1,800</b>

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Notes:

1. The number of members relates to members of each reporting provider and should not be taken as numbers of individuals, since individuals can have more than one pension provider.
2. Employer sponsored schemes include contracts for schemes nominated by employers or set up under a trust by an employer.
3. Non-Employer sponsored schemes are contracts set-up by a financial institution and offered for sale to the public, and include schemes arranged via Trade Unions or other bodies.

**Please note:** ASHE data is derived from a survey that counts main pension memberships as at April of each year. HMRC data is derived from administrative sources and include all memberships within a financial year. There is some double counting in this data as individuals who have both a personal pension and a stakeholder pension will be double counted within the HMRC data, and individuals who have both an occupational pension and a stakeholder/personal pension will be counted in both the ASHE and HMRC data. Therefore, figures in the above tables should not be added together.

### 2.3 What is the population's ability to understand financial notions related to pensions? (for instance compound interests, ...)

The Financial Services Authority commissioned the Financial Capability Baseline Survey to inform its strategy on improving peoples' level of financial capability, by establishing the current state of financial capability in the UK and providing a baseline against which to measure future progress<sup>24</sup>. The survey was developed, analysed and reported by the Personal Finance Research Centre at the University of Bristol. The survey was carried out in 2005 and the report<sup>25</sup> was published in March 2006.

The main findings were:

- a) Many people are failing to plan ahead adequately for retirement or for an unexpected expense or drop in income:
  - 43 per cent of people have no savings at all - this is not a case of people failing to do so simply because they do not have enough money since many people at all income levels are not planning ahead, while plenty of people with very low incomes do;
  - 81 per cent under state pension age think that a state pension will not provide them with the standard of living they hope for in retirement but only 37 per cent of these have made any additional retirement provision;
  - 55 per cent of those under SPA agree with the statement 'I would rather have a good standard of living today than plan for retirement';
  - 65 per cent over SPA have some non-state pension provision;
  - 79 per cent over SPA said their income was adequate for their desired living standard.

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<sup>24</sup> They have suggested that the survey should be repeated every 4-5 years but have not made a firm funding or commissioning commitment.

<sup>25</sup> Consumer Research 47 Financial Services Authority, "Levels of Financial Capability in the UK :Results of a baseline survey". See: <http://www.fsa.gov.uk/pubs/consumer-research/crpr47.pdf>

- b) Many people do not take adequate steps to choose financial products to meet their needs:
- Most households buy financial products and services, yet many do not shop around or seek the right information to find a good deal;
  - 21 per cent who made a purchase in the last five years made a decision without seeking any advice or information from anywhere;
  - People usually learn from experience: in general, with more products held, choosing patterns improve;
  - Those least likely to shop around were in social grades DE, in lower income bands and aged 18-24.
- c) Adults aged under-40 are less financially capable, on average, than their elders:
- This is true even after taking into account factors such as their lower average incomes and relative inexperience in dealing with financial institutions;
  - Adults aged under-30 are the least capable;
  - Age has a much higher impact on capability in planning ahead than income.

Other areas of interest covered by the survey include the use of advice in choosing products, preference for risk with investments and a financial capability "quiz".

**Annex D** also provides some of the results of the financial "quiz" on financial concepts that have relevance to pensions saving, namely: interest rates, inflation and return on investment.

## 2.4 What are the main tools to provide information to individuals?

In January 2007, the UK Government published its long-term approach to Financial Capability<sup>26</sup>, setting out its aspirations for the next 10-20 years. A wide range of organisations in the public, private/financial services industry and voluntary sectors, is involved in providing information and services or running initiatives to help individuals understand and manage their finances in the UK. **Annex E** provides some examples (extracted from Financial Capability: the Government's long-term approach - summary of responses<sup>27</sup>).

The Government's overall aim is to ensure people have the financial skills and advice to enable them to understand and manage their financial affairs and make effective decisions about their money, including retirement planning. The Government will publish its financial capability action plan in Spring 2008, which will show how financial capability can be integrated into tools, information products and services. The Government recognised that supporting people in building

<sup>26</sup> [http://www.hm-treasury.gov.uk/media/1/F/fincap\\_150107.pdf](http://www.hm-treasury.gov.uk/media/1/F/fincap_150107.pdf)

<sup>27</sup> See: [http://www.hm-treasury.gov.uk/media/4/2/consult\\_fincap\\_resp240707.pdf](http://www.hm-treasury.gov.uk/media/4/2/consult_fincap_resp240707.pdf) for full report.

financial capability - the knowledge, skills and confidence to support better financial decision-making - is important in promoting personal responsibility for retirement. And this encourages sustainable independence and material well-being in later life.

The Government's approach is wide ranging and aims to ensure that:

- All adults in the UK have access to high-quality generic financial advice to help them to engage with their financial affairs and make effective decisions about their money;
- All children and young people have access to a planned and coherent programme of personal finance education, so that they leave school with the skills and confidence to manage their money well; and
- A range of Government programmes is focused on improving financial capability, particularly to help those who are most vulnerable to the consequences of poor financial decisions.

The UK Government and the Financial Services Authority (FSA) have worked closely together on financial capability and Government continues to support the FSA-led National Strategy for Financial Capability. Following the publication of its baseline survey of financial capability in March 2006, the FSA is delivering measures designed to improve people's understanding of their finances, focusing on schools, higher education and the workplace:

- **Schools:** how the curriculum can deliver improved levels of financial capability. Target: 500 schools signed up to *Learning Money Matters*<sup>28</sup> by 2010 (350 by December 2006).
- **Young Adults:** helping them make sense of money. Target: All major organisations providing services to young people communicate some basic financial capability pointers and messages to their clients by 2008.
- **Workplaces:** exploiting their potential to reach 28 million employees at a time and place convenient to them and to provide them with support from trusted sources (their employers and trade unions). National rollout of Make the Most of Your Money<sup>29</sup> initiative in 2007.

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<sup>28</sup> *Learning Money Matters* is a **pfeg** initiative aimed at increasing the visibility and quality of personal finance education in secondary schools in England so that all young people will leave school with the financial knowledge, skills and confidence they need to live full adult lives. For full details see: [pfeg - Developing financial capability in young people](#)

<sup>29</sup> The *Making the most of your money is an FSA* programme and delivers free financial education to employees in the form of an hour-long seminar in the workplace, delivered by specially trained volunteer presenters. Employees also receive a financial information pack building on the seminar content, which covers budgeting, saving and investing, borrowing, dealing with problem debt, protecting what you have and planning for retirement. For full details see: [http://www.fsa.gov.uk/financial\\_capability/pdfs/workplace.pdf](http://www.fsa.gov.uk/financial_capability/pdfs/workplace.pdf)

### 3. Session three: Informing on rights

#### 3.1 What do individuals know of their already accrued pensions including statutory pensions (unfunded and funded tiers)?

As part of the Department for Work and Pensions research programme, independent evaluations<sup>30</sup> were carried out with individuals who had received a Combined Pension Forecast (CPF), a document which shows an individual's projected income in retirement, combining their current occupational or personal pension forecast; together with their state pension forecast. These evaluations consisted of a quantitative survey with around 5,000 CPF recipients and a prior qualitative study with CPF providers (employers) and recipients (employees).

Findings from the survey show that around half of CPF recipients reported that they had at least a reasonable knowledge of what their retirement income would be<sup>31</sup>. The level of knowledge tended to increase with age.

Furthermore nationally representative evidence in the 2006 attitudes to pensions survey<sup>32</sup> found that when respondents were asked to assess their own knowledge of pension issues, a quarter (25 per cent) said they knew little or nothing about pensions issues. A further 40 per cent said their knowledge of pension issues was patchy and they knew what concerned them but no more. Three in ten (30 per cent) described themselves as having reasonable, basic knowledge of pensions, they knew how they work generally, but didn't understand the details. Just five per cent felt they had a good knowledge of pension issues.

It also found that 32 per cent of individuals recalled receiving a State Pension Forecast (SPF). Two-thirds (66 per cent) of respondents who recalled receiving a SPF understood all or most of it and 76 per cent found this information useful.

DWP has also commissioned qualitative research to be conducted with nearly 80 people who had recently been sent either an Automatic Pension Forecast issued by The Pension Service (DWP) or a Statutory Money Purchase Illustration (see Private Pension Annual Statements in our response to question 3.3) issued by a private pension provider. The research gives a deeper level of understanding of the way people responded to pension forecasts and the reasons behind the actions they may or may not have taken. We anticipate the report will be published in May 2008 and will be freely available from the DWP website<sup>33</sup>.

<sup>30</sup> Full findings from these reports can be found by clicking on the following links:

- [DWP research report 293: Combined Pension Forecasts - a survey of their impact on recipients](#)
- [DWP research report 212: Combined Pension Forecasts - a report on the experiences and views of CPF providers and recipients](#)

<sup>31</sup> We cannot generalise these findings more widely as evidence shows that those with private pensions have higher levels of knowledge, and are more likely to engage with pensions those without a private pension provision.

<sup>32</sup> 'Attitudes to pensions: the 2006 survey by Clery et al. DWP research report number 434. Published in 2007.'

<sup>33</sup> <http://www.dwp.gov.uk/asd/asd5/rrs-index.asp>.

## Protecting members' pension rights

Since the 2004 Pensions Act, (and due to the collapse of a number of pension schemes)<sup>34</sup> the UK Government has introduced the Pensions Regulator and the Pension Protection Fund (PPF). Both bodies play a key part of the Government's strategy to restore security and public confidence in the pension system.

The Pensions Regulator helps protect members of all work-based pension schemes by:

- protecting the benefits of members of work-based pension schemes,
- concentrating its effort on schemes where it assesses that there is a serious risk to scheme funding, or a high risk of fraud,
- promoting the good administration of work-based pension schemes; and
- reducing the risk of situations arising that may lead to claims for compensation from the PPF

The Pension Protection Fund (PPF) is an independent body which will protect members of eligible defined benefit/final salary schemes by paying compensation if their employer becomes insolvent and the pension scheme is under funded. The PPF is funded by a levy on pension schemes. The Financial Assistance Scheme (FAS) provides support to qualifying members of defined-benefit occupational pension schemes which started to wind up, underfunded, between 1 January 1997 and 5 April 2005 before the PPF was set up. It is funded by the taxpayer.

Both the PPF and FAS provide help that is broadly equivalent to 90% of the member's expected pension.

In December 2005 new scheme funding requirements took effect. As part of these new arrangements schemes now have to provide members with much more information about the way the scheme is funded. At regular intervals members have to be provided with a summary funding statement. Other more detailed information about the way the scheme is funded has to be provided on request.

### 3.2 What do people know of the impact of different decisions on retirement age and transition from work to retirement on their potential future benefits?

Qualitative research with older workers suggests that those who had not planned for retirement felt that they should have put plans in place but hadn't got round to it, or could not afford to. Others had other priorities or did not believe in planning for the future. Those who did plan for retirement had a clear idea of when this would be and how they would support it. Many had started to plan as a result of an improving financial situation, and those who had planned were generally more happy with their retirement income<sup>35</sup>.

<sup>34</sup> For example ASW and UEF

<sup>35</sup> DWP RR 281 'Factors affecting the labour market participation of older workers: qualitative study'

Analysis of both when people in work expect to retire, and the retirement decisions of retired people suggests that the State Pension Age (SPA) has an important impact on retirement behaviour, both as an age which shapes expectations and as the first opportunity to draw state pension. Of those in work, 39 per cent of those planning to retire at SPA said that this was because it is the first opportunity to draw state pension, and 57 per cent had always expected to retire then.<sup>36</sup> Of those who had retired at SPA, around half gave each of these reasons.

Research findings from the 50+ Face to Face Guidance Project pilots (see our response to Question 1.1) that are due to end March 2009, will inform the development of best practice for Government and non-government organisations to use in the guidance that they offer older workers. The pilots are only just starting their operational phase, so no evaluation data is yet available.

### 3.3 What are the main tools to provide information to individuals?

The United Kingdom provides a number of specific forecasting products to provide information to people on likely income in retirement.

#### State Pension Forecasts

- Individual Pension Forecasts (IPF). These are detailed and personalised forecasts that are provided "on demand". Individuals need to supply information about their own specific circumstances. This enables the inclusion of information on how future changes to an individual's circumstances will impact on their future State Pension provision, for example, delaying retirement or a change in their own earnings level.
- Real Time Pension Forecasts (RTPF). This is a web-based forecasting service introduced in October 2004. It provides personalised forecasting information similar to IPFs but does not include all of the IPF features available.
- Combined Pension Forecasts (CPF). This is a voluntary service which involves occupational and personal pension schemes working in partnership with Government to present a picture of State and Private pension together in the same annual statement. The statements themselves are issued by the participating scheme. They are designed to prompt people to consider their pension provision and review their plans. This service was introduced in October 2001.

Customers receive a leaflet (BR19L) with their pension forecast. This provides detailed information on State Pensions and the factors that can affect their entitlement. It also sign-posts to sources of further information; e.g. Pension Centres and Pensions Information Line.

However, State Pension reforms contained in the Pensions Act 2007 require some significant changes to the pension forecasting IT systems. Until these changes can be made, we have introduced a number of temporary changes regarding the availability of pension forecasts and the services provided to help people to plan for retirement.<sup>37</sup>

<sup>36</sup> DWP research report 200 'Factors affecting the labour market participation of older workers'

<sup>37</sup> People who reach State Pension age before 6 April 2010 can continue to request a state pension forecast as normal (either online, in writing or over the phone). We are temporarily unable to provide people who reach state pension age on or after 6 April 2010 with a full state pension forecast. However, we are providing personalised

## Private Pension Annual Statements

### Defined Contribution Schemes

Legislation requires that scheme members must be sent an annual benefit statement that includes information on the current fund value. In addition, members must receive a statutory money purchase illustration that provides an estimate of how much pension they may receive at the scheme retirement age based on certain prescribed assumptions.

### Defined Benefit Schemes

Defined Benefit schemes are required by legislation to provide "on request" certain information, including the amount of pension that may be payable based on current scheme membership or service projected to scheme pension age. However, many schemes provide annual statements voluntarily.

The Financial Services Authority provides the guide "Important information about your yearly pension statement" for general information for consumers about pension statements<sup>38</sup>.

### Retirement planning tools

A number of UK organisations including the Financial Services Authority, organisations in the voluntary sector and various providers of DC and DB schemes provide online planners or ready-reckoners to simulate different retirement planning scenarios such as increasing contributions, retiring later.

As part of the Government's long term approach to Financial Capability<sup>39</sup>, HM Revenue and Customs and DWP are jointly developing a 'retirement planner'. The new planner (which will be targeted at people in pre-retirement from around aged 50), will be available as a paper guide and as a web-based tool and will be launched in spring 2008. The planner aims to help people approaching retirement without adequate pension provision find ways to maximise their retirement income by signposting them to sources of help information and guidance about:

- taxation issues in retirement,
- working in retirement,
- benefits; and
- other issues of particular interest to those with low projected retirement incomes.

Previously, DWP carried out small scale qualitative research<sup>40</sup> (in 2006) to explore needs, preferences and expectations regarding on-line retirement planning tools.

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information to this group, including details on the number of qualifying years people have, to help with considerations such as the payment of voluntary National Insurance contributions, and how the changes to the State Pension rules may affect their State Pension position. These services help people to continue to plan for their retirement. Combined Pension Forecasts are not being issued to anyone while the forecasting IT is being updated to reflect the reform changes. It is anticipated that all system changes will be in place by Autumn 2008.

<sup>38</sup> See: [http://www.moneymadeclear.fsa.gov.uk/pdfs/pension\\_statement.pdf](http://www.moneymadeclear.fsa.gov.uk/pdfs/pension_statement.pdf)

<sup>39</sup> [http://www.hm-treasury.gov.uk/media/1/F/finicap\\_150107.pdf](http://www.hm-treasury.gov.uk/media/1/F/finicap_150107.pdf)

<sup>40</sup> DWP Research Report Number 413: Needs and preferences among moderate to low earners for retirement information on line: small scale qualitative research. See: Summary: <http://www.dwp.gov.uk/asd/asd5/summ2007-2008/413summ.pdf>

The research found that:

- Overall, findings suggest participants found retirement planning difficult and that they would welcome help in this task.
- In particular, participants would like help to establish desired retirement income, project what they are likely to get from current provision and calculate how much more they would need to save to meet their aspirations.
- There was a broadly positive reaction to the concept of an online retirement planning service but it was recognised that it would not be suitable for all.

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Report: <http://www.dwp.gov.uk/asd/asd5/rports2007-2008/rrep413.pdf>

## Annex A

Summary of emerging research findings  
 Individuals' attitudes and likely reactions to the personal account reforms 2007:  
 a quantitative survey

### SUMMARY OF EMERGING RESEARCH FINDINGS

#### INDIVIDUALS' ATTITUDES AND LIKELY REACTIONS TO THE PERSONAL ACCOUNT REFORMS 2007: A QUANTITATIVE SURVEY

Patten Smith, Caroline Webb, Julia Pye, Rea Robey, David Jeans

##### Summary

Emerging findings from a nationally representative survey of individuals' attitudes and likely behaviour in response to automatic enrolment into a qualifying workplace pension scheme, a minimum employer contribution and the setting up of a new personal accounts scheme, show:

- There is considerable public support for the reforms:
  - The majority of people (64%) found the idea of automatic enrolment attractive.
  - Most people (91%) found the idea of an employer contribution attractive.
- Seven in ten (69%) people likely to be eligible for automatic enrolment under the Government's proposals said that, if enrolled into personal accounts, they would be likely to remain in the scheme. Just over two in ten (22%) said they would be likely to opt out.
- The employer contribution and the ease of saving are key reasons for people saying they would participate if they were enrolled into personal accounts.

This note presents some of the key findings that are starting to emerge from this survey. Analysis is continuing, and it is currently anticipated that a full report of findings will be published in spring 2008.

##### Background to the research

This research forms part of a wider programme of research and analysis to inform the Government's proposals to encourage and enable more people to save for their retirement.

This survey was designed to gather evidence on public attitudes to key aspects of the pension reforms, such as automatic enrolment, and to provide

estimates of the likely behaviour of individuals if they were automatically enrolled into a personal account<sup>1</sup>.

This programme of research includes a parallel nationally representative survey of employers' attitudes and likely reactions to the personal account reforms<sup>2</sup>.

### **Methodology**

This research is being carried out by Ipsos MORI on behalf of the Department for Work and Pensions (DWP). It involves a nationally representative quantitative survey of individuals in Great Britain who would be eligible for automatic enrolment under the Government's proposals<sup>3</sup>. Face-to-face interviews were carried out with 754 individuals in their own homes, between July and September 2007.

In view of the complexity and unfamiliarity of the topic, an extensive initial development and piloting phase was carried out. This phase informed the design and wording of the questionnaire and the detailed and tailored information about automatic enrolment, contribution levels etc. that was provided during the interview. This was to ensure that respondents were able to give informed responses on likely behaviour.

### **Emerging findings**

This note presents some of the findings that are starting to emerge from this research. Analysis of the findings is ongoing, and it is currently anticipated that a full report of findings will be published in spring 2008.

### **Support for the reforms**

- The majority of people (64%) found the idea of automatic enrolment attractive.
- More than seven in ten people (72%) found the idea of automated individual contributions attractive.

<sup>1</sup> Employers with a pension scheme meeting qualifying tests will have a choice over whether to enrol eligible employees into their own pension scheme or the new personal account pension scheme. However, to make it easier for people to relate to, this survey mainly focused on the situation whereby people would be automatically enrolled into personal accounts, as the people surveyed were not members of a workplace pension scheme and might not have had access to an employer scheme.

<sup>2</sup> Grant C, Fitzpatrick A, Sinclair P and Donovan JL, forthcoming in 2008, *Employers' attitudes and likely reactions to the personal account reforms 2007: Report of a quantitative survey*. A summary of key findings emerging from this survey can be found at <http://www.dwp.gov.uk/pensionsreform/factsheets.asp>

<sup>3</sup> Specifically, the survey interviewed employees aged between 22 and state pension age who were earning at least £5,000 per year from a single job in the private sector, and did not have a pension that their employer contributed to.

- Most people (91%) found the idea of an employer contribution attractive.

**Participation levels**

- Seven in ten people (69%) said that, if enrolled into personal accounts they would ‘definitely’ or ‘probably’ stay in the scheme.
- Just over two in ten (22%) said that, if enrolled into personal accounts, they would ‘definitely’ or ‘probably’ opt out, and 10% said ‘it depends’ or that they did not know what they would do.
- Those aged 50-64 were significantly more likely to say they would opt out than those aged under-40.

**Table 1 Participation levels analysed by age group**

	Definitely opt out	Probably opt out	Probably stay in	Definitely stay in	It depends / Don't know
<b>ALL</b>	11%	11%	45%	24%	10%
<b>Age 20-29</b>	5%	9%	49%	26%	11%
<b>Age 30-39</b>	9%	8%	50%	26%	7%
<b>Age 40-49</b>	9%	12%	44%	25%	10%
<b>Age 50-64</b>	21%	14%	34%	19%	12%

Base: All respondents

**Reasons for remaining in the scheme or opting out<sup>4</sup>**

- Those who said they were likely to remain in the scheme if enrolled into personal accounts said that this was because:
  - They needed to start saving for retirement (49%)
  - The scheme seemed like an easy way to save (31%)
  - They wanted their employer to contribute to their pension (31%)
- Those who said they would be likely to opt out said this was because:
  - They would rather save in a different way, other than in a pension (27%)
  - They already had a personal pension (16%)
  - They were too old to start saving (16%)
  - They couldn't afford to save (16%)

<sup>4</sup> Respondents were able to give more than one reason, and their answers were unprompted. The following section shows key responses that were given by at least 10% of respondents.

- They were concerned about the return on investments/ potentially losing their money (12%).

### Contributions

- Of the people who said they might remain in the scheme if enrolled into personal accounts, just under half (46%) said they were likely to contribute above the minimum level on a regular basis<sup>5</sup>. Of these:
  - More than half (54%) said they would make contributions of 5% or 6%
  - Around two in ten (21%) said they would make contributions of between 7-9%
  - A further two in ten (19%) said they would make contributions of between 10-20%.
- Thirteen per cent of those who said they might remain in the scheme said they would like to pay in the occasional additional lump-sum rather than making higher regular contributions.
- Analysis shows that overall, only a small minority (3%) of those who said they would stay in personal accounts might be likely to exceed the £3,600 annual limit on contributions<sup>6</sup>.

### Investment choice

- Of those who said they were likely to remain the scheme if enrolled into personal accounts, the majority (68%) said they would choose how to invest their money. However, other research on investment behaviour shows that, in practice, inertia means that the majority of pension scheme members end up in a default fund<sup>7</sup>.
- Of those who said they would choose how their money is invested around seven in ten (68%) said that the level of return was the most important issue for them. However, a significant minority (23%) said they were interested in ethical investment options regardless of the level of return.

### Attitudes to investment risk

The survey included a question designed to enable calculation of each respondent's attitude to investment risk based on a standard measure of

<sup>5</sup> Respondents were told that those who take part in the scheme will be required to save a minimum of 4% of whatever they earn between around £5,000 and £33,500.

<sup>6</sup> This analysis excludes those who said they might like to pay in the occasional additional lump-sum

<sup>7</sup> Cronqvist & Thaler, 2004, *Design choices in privatized social-security systems: Learning from the Swedish experience* Papers and Proceedings of the 116<sup>th</sup> Annual Meeting of the American Economic Association

“constant relative risk aversion” (CRRA). This technique has been developed by economists and is used in the financial industry to identify risk preferences in relation to financial products.

This question asked respondents to imagine a situation in which:

- they had a sum of money to invest for their retirement;
- they were offered an investment opportunity with “a well-known bank” where there was an equal chance of doubling their money or losing a third of the amount invested;
- they could invest all, some, or none of their money in the investment opportunity described and;
- any money not invested in this opportunity would be placed in a savings account giving a 3% yearly return.

The proportion of their money they decided to invest was then used to calculate their ‘risk attitude’ (CRRA) score. People who were not willing to invest any of their money, or only a very small proportion of their money, in the investment opportunity were classified as being “risk averse”. Those willing to invest larger amounts of money were classified as being “risk loving”.

- Based on their response to this scenario:
  - Over four in ten respondents (44%) were classified as ‘risk averse’ i.e. they were not keen on risking substantial amounts of their money for the potential of a higher return.
  - About two in ten (17%) were classified as being very mildly risk averse.
  - Almost three in ten (29%) were classified as being ‘risk loving’.

## Annex B

### Pensions Education Fund (PEF) – brief summary

DWP, through the Pensions Education Fund, has offered funding to local and national not-for-profit organisations (such as trades unions, charities, trade associations and the voluntary sector) to use innovative ways to increase financial awareness and encourage working people to provide for their retirement. The principle of the fund is to provide impartial and accurate information on pensions and retirement planning to individuals (employees and self employed people) in the workplace, where practicable and feasible.

The Fund is a UK wide initiative established to ensure that individuals, particularly the traditionally hard to reach groups who are at risk of under saving, have information and support to make an informed choice about the retirement income they want and how they can achieve it.

In all 26 organisations are receiving funding which started in January 2006 and will end in March 2009. These projects are delivering information using a variety of methods including group events, one to ones, websites, CDs, information booklets/packs and by training intermediaries and union members (for example Trade Union Pensions Champions) who return to the workplace and cascade information.

DWP commissioned an independent research organisation to carry out an evaluation of fund initiatives to:

- Explore the impact of the fund initiatives on individuals' knowledge and attitudes towards planning for retirement and on savings behaviour;
- Provide evidence to help assess the potential role that a trusted third party can play in delivering pensions information; and
- Explore providers' experiences of setting up and running the initiatives.

Research has been conducted with 14 of the 26 PEF schemes, these were selected to ensure coverage of a range of different types of initiatives. Interviews were carried out to collect detailed information on providers' experiences of setting up and running particular initiatives, on employers' experience of participating, and on the influence that funded activities have had on individuals' attitudes to retirement planning and saving for retirement.

A DWP research report on the evaluation will be published in summer 2008.

## Annex C

### Information products<sup>41</sup> on pension issues at 22<sup>nd</sup> June 2007

	Product	Delivery body	Channel type	Purpose	Impact to date
1	State Pension forecasts	The Pension Service	Paper-based and online	Provide individuals with estimates, in today's money values, of the amount of State Pension they are likely to get based on their NI contributions so far.	18m forecasts sent but no evidence of changing behaviour, high deadweight, low levels of readership when unsolicited (31%)
2	Generic Leaflets	DWP/TPS	Paper-based and online	Information guide eg "Pension the Basics", providing a general introduction to the subject of pensions, the state pension system and so on	Unknown but unlikely to prompt hard actions based on APF evidence
3	Pensions Education Fund pilots	DWP	Workshops, presentations, one-to-one information sessions, written information packs, websites and CDs/DVDs	Aiming to increase financial awareness and encourage working people to provide for their retirement by capitalising on the relationships between employees/self employed people and 'trusted third parties' in the provision of pension information.	On-going evaluation, findings Sept/Oct 2007

<sup>41</sup> Note that the table focuses specifically on information products for individuals and excludes any products relating to regulated financial advice.

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	Product	Delivery body	Channel type	Purpose	Impact to date
4	Legal information requirements for occupational pension schemes	Any providers of occupational schemes	Online and/or paper-based	<p>The 1995 Pensions Act requires occupational pension schemes to provide their members with:</p> <p><b>basic information</b> about the scheme to prospective scheme members within 2 months of joining the scheme; existing members, their spouses, beneficiaries and trade union representatives can request such information to be made available to them within 2 months of being requested.</p> <p><b>information about their rights and benefits</b> when requested</p> <p><b>statements of benefits and access to regular reports</b> about the scheme. Members of a money purchase occupational scheme should be provided automatically with an annual statement within 12 months of the end of the scheme year</p> <p>Members of a final salary occupational scheme have the right to request a statement of their estimated pension at their normal retirement date. Once requested, a statement should be provided within 2 months.</p>	n/a – aim to meet “duty of care/legal minimum”?
5	Statutory Money Purchase Illustrations	Any providers of DC schemes	Mostly paper-based (though possible online)	Pension providers are required to provide members of DC schemes with yearly illustrations expressed in today's prices in order to give them an idea of expected income at retirement.	Unknown
6	Annual Benefit Statements	DB scheme administrators	Mostly paper-based (though possible online)	Projections sent (usually annually –although not mandatory) to members of Defined Benefit schemes to provide them with an idea of the pension benefit they should expect at retirement	Unknown
7	Providers/ schemes' online planners or ready-reckoners	Any providers of DC and DB schemes on a 'voluntary' basis	online	Provide their members online facilities to simulate different retirement planning scenarios such as increasing contributions, retiring later	Unknown due to confidential commercial information, [Tesco's Smarter Money site received 72,000 visits per month when assessed in Aug 2005]

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	Product	Delivery body	Channel type	Purpose	Impact to date
8	The Pension Advisory Service	TPAS	Phone (helpline), online and paper-based information (eg leaflets)	Provide free information, advice and guidance on the whole spectrum of pensions covering State, company, personal and stakeholder schemes including written communication for private pension disputes. The TPAS website has a ready-reckoner enabling online users to calculate their new state pension age based on the White Paper recommendations: <a href="http://www.pensionsadvisoryservice.org.uk/state_pensions/spa_calculator/">http://www.pensionsadvisoryservice.org.uk/state_pensions/spa_calculator/</a> (TPS also has an online SPA calculator)	About 55,000 calls a year
9	Financial Services Authority	FSA	Online (via money made clear website), leafletline and customer contact number	Provide tools and information to help and support consumers on issues such as: <ul style="list-style-type: none"> <li>▪ shopping around and comparing the features and costs of financial products using comparative tables;</li> <li>▪ planning finances;</li> <li>▪ keeping up to date with latest warnings and alerts;</li> <li>▪ find FSA online publications;</li> <li>▪ check that a firm consumers are dealing with is authorised by the FSA.</li> </ul>	Unknown
10	ABI/FSA pension calculator	FSA and ABI	online	Tool to help people work out how much retirement income an individual might receive from the amounts he/she save	About 266,000 visits in the year to May 2007
11	Stakeholder pension decision tree	FSA	online	There are 2 decision trees, one aimed at employers to decide whether they are legally obliged to provide a stakeholder scheme and; one aimed at individuals to decide whether they should take up a stakeholder pension	79% of users achieved an outcome using the decision trees, almost ¾ of respondents said that they would take some follow-up action (FSA quantitative research, June 2000)
12	National campaign	DWP, TPS	TV, radio and/or newspaper ads	Inform and/or educate and/or promote behaviour change	Effectiveness is difficult to measure

## Annex D

### Extracts from financial capability quiz

#### (Levels of Financial Capability in the UK Results of a baseline survey)<sup>42</sup>

Six of a total of eight 'money quiz' questions were posed to respondents to test elements of applied financial literacy. Unlike other areas of the questionnaire, they all had a correct answer that could be scored. These questions were devised by the FSA to capture a range of applied financial literacy competences that are needed by individuals in dealing with their finances.

The first task in the 'money quiz' section was to read out the final balance from a bank statement. Respondents were free to give any answer, and most were correct. Fewer than one in ten respondents (nine per cent) answered this question incorrectly.

Respondents were asked '*If the inflation rate is 5% and the interest rate you get on your savings is 3%, will your savings have at least as much buying power in a year's time?*' to assess their understanding of the effects of inflation and percentages. Again it required a yes/no answer. More than one in five (21 per cent) of all respondents did not give the correct answer, but this proportion almost doubled amongst 18- to 20-year-olds (41 per cent of whom did not answer correctly). In contrast, only 14 per cent of respondents in their fifties failed to give the correct answer. Once again there was a link with income, with the incidence of incorrect replies being highest amongst those on the lowest incomes; the proportions across the quintiles ranged from 29 per cent to 12 per cent not giving the right answer. Women were also less likely than men to know the answer (26 per cent and 17 per cent respectively).

Two questions were designed to capture people's ability to use an illustration in the form of a graph to be able to spot the best returns on three different investments. In this case, a quarter of people were unable to give the correct reply to each of the two questions (25 and 26 per cent respectively). Interestingly the proportions of 18- to 20-year-olds not getting the answer right did not vary by more than two percentage points from this average. Respondents aged 70 and over, however, were least likely to choose the best fund in either question (40 per cent and 39 per cent respectively). This contrasts notably with the proportion of those in their thirties who failed to choose the right answers (in each case 20 per cent did so).

Basic arithmetic was tested in the final question, where respondents were asked whether a cash discount of £30 was better than a ten per cent discount on a television with an original price of £250. Here, one in ten (ten per cent) failed to give the correct reply. There was little difference in the proportions getting the question right across the age bands from 18 to 60. However, respondents over the age of 60 were slightly less likely to give the correct answer, and one in five (20 per cent) of those aged 70 and above chose the wrong answer. The proportion of respondents struggling with this question was clearly associated with income. Just three per cent of those respondents with the highest household incomes answered it wrongly, compared with 16 per cent of those in the lowest-income bracket.

We also asked all respondents which of seven types of savings could be directly affected by stockmarket performance. We scored this question between 0 and 1, with a score of 0.2 for each product correctly identified, in order to capture some level of capability even when respondents

<sup>42</sup> Consumer Research 47 Financial Services Authority, "Levels of Financial Capability in the UK :Results of a baseline survey". See: <http://www.fsa.gov.uk/pubs/consumer-research/crpr47.pdf>

had missed one or more products. This question was clearly the most difficult, and on average respondents scored 0.36. The youngest respondents scored an average of just 0.19, and the higher-scoring 50- year-olds still only managed an average of 0.44. The oldest respondents did not fair as badly as the youngest, but achieved average scores of just 0.29.

As we note above, we combined the replies to the financial literacy element of the quiz into an overall score, with a maximum score of six. The average overall mark for the quiz was 4.9 out of six. Forty- to fifty-year-olds scored the highest of all the age bands, on average, at 5.2. Men scored slightly more than women (5.1 and 4.8 respectively), and respondents interviewed in Northern Ireland scored less than those in the other countries, at just 4.7. Respondents with household incomes in the lowest two quintiles scored below average in the quiz (4.5), and the average score increased with income; those with the highest incomes scored an average of 5.5.

## Annex E

Examples of financial capability information, services and initiatives (extracted from Financial Capability: the Government's long-term approach - summary of responses<sup>43</sup>).

The Third Sector and NDPBs responded as follows:

- “Good examples are the AXA Avenue programme and Pfeg case studies.
- Examples such as National Debtline have been positive in relation to the impact of advice both on clients’ health and well-being and on their ability to maintain debt repayment arrangements and avoid further debt going forward.
- We would recommend an initiative called ‘MoneyHelp’ which was piloted in Edinburgh and Calderdale, delivering outreach sessions face-to-face in the community with specific target profiles for the hardest to reach. The pilot has been expanded across 7 areas in England, Wales and Scotland focusing on the two strands of community outreach and in-school provision.
- ABCUL produces a range of financial literacy leaflets free to their members and communities. Since 2002 over 1.2 million have been distributed and since 2006 they have included saving, budgeting and dealing with debt. Anecdotal evidence suggests that these leaflets are very popular demonstrated by the number of repeat orders and their use in information packs.
- The ‘Financial Skills for Life’ programme which works with mainly socially excluded groups was independently evaluated and evidence showed genuine outcomes in terms of improved budgeting and borrowing performance by people who attended financial capability sessions.
- The Young Scot InfoLine - a phone and web-based information service for young people aged 16-26. Young Scot’s evaluation of their system found that young people made calls primarily between 12 noon and 8 pm, and that a package of communication mechanisms worked best - telephone, web, instant messaging and email.”

The financial services industry and other private sector organisations responded as follows:

- “The Face2Face with Finance education programme helps young people aged 11-18 improve their financial capability. It provides a range of curriculum linked materials for use in secondary schools. Conclusions after 13 years show: firstly that financial education needs to be tailored and secondly success is based on three factors – space in the curriculum, good quality teaching resources and confident teachers.
- The Citizens Advice Bureau “Financial Skills for Life” programme where individuals have significantly improved their ability to budget and save. The evaluation highlighted that it

<sup>43</sup> See: [http://www.hm-treasury.gov.uk/media/4/2/consult\\_fincap\\_resp240707.pdf](http://www.hm-treasury.gov.uk/media/4/2/consult_fincap_resp240707.pdf) for full report.

was more effective to make training tangible and relevant to participants' own situations so beneficiaries could put information into practice and that structured training should be flexible enough to cater for the needs of individual target groups.

- The Barclays Horizons programme, which by end 2006 had helped over 30,000 lone parents and their children with support ranging from financial literacy training, to debt advice and to actual financial support towards education related costs.
- Also the NCH Financial Futures programme which is helping excluded groups across the UK improve their money management skills to help secure financial stability.
- The successful pilot between the Citizens Advice Bureau and IFAs which focused on generic financial advice on "lower" income groups incorporating work on savings products like the Child Trust Fund and pensions.
- We believe the biggest difference is made where people receive trusted advice eg The Pensions Advisory Service, whereas the provision of information eg pension forecasts, appear to have limited impact.
- The Government has introduced a number of very good initiatives such as the ISA, Child Trust Fund and Savings Gateway and there has been success in sustaining and creating asset ownership across the socio-economic spectrum."