Summary
• Five million gig economy and self-employed workers are not covered by auto-enrolment.
• Phased retirement will become increasingly common, partly due to insufficient saving.
• Drawdown followed by an annuity in later years is emerging as a common decumulation choice.

Hard labour

Modern working practices – from the rise of the gig economy to phased retirement – mean traditional pension products are becoming a poor fit for many people. Alastair O'Dell investigates the innovations taking place to meet emerging needs

The so-called 'snowflake generation' certainly have legitimate cause for complaint when it comes to their retirement prospects. High housing costs and university debts are eroding the ability to save just as unstable working conditions limit the ability to earn.

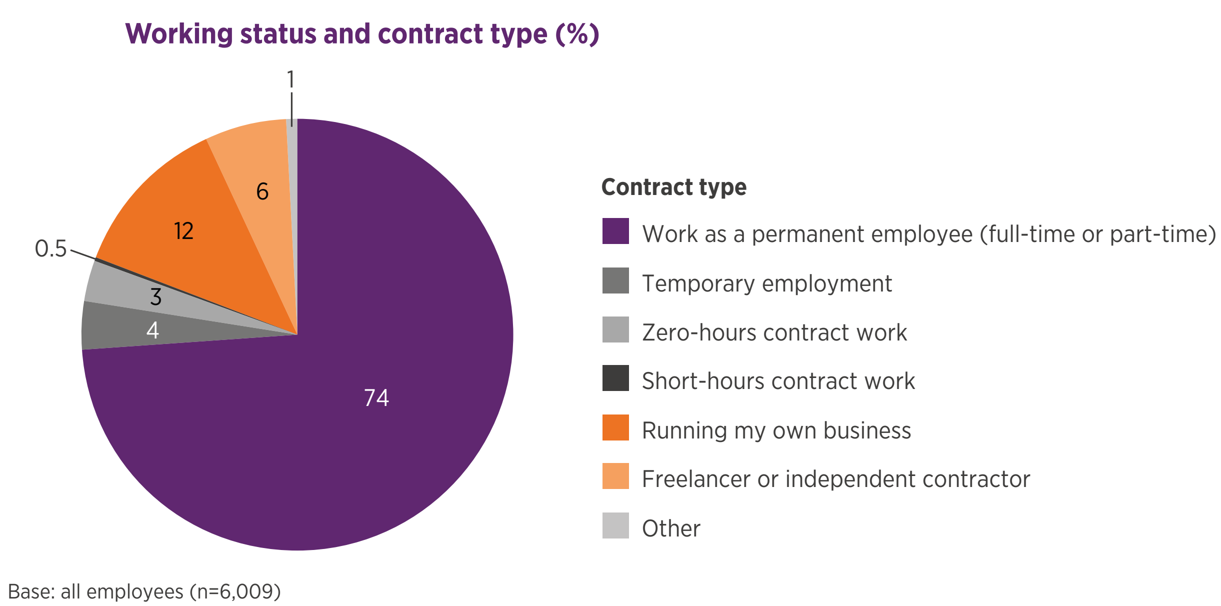
Those new workers are much more likely than existing workers to partake in much wider trends; periods of self-employment and the rise of the 'gig economy'. A CIPD report found that 26 per cent of the working population are now not formally employed *[see chart below]*.

While employees must be auto-enrolled into an eligible pension scheme with employer contributions of 2 per cent, rising to 3 per cent in April 2019, there is no provision for informal workers. Those workers would need to contribute the entire combined figure (including tax relief) of 5 per cent, rising to 8 per cent in April 2019 themselves, to be saving the same amount for retirement as workplace employees. But even these rates are insufficient – the PLSA recommended combined contributions of 12 per cent by 2030, with a 50/50 split, in its July report.

Nest head of pensions solutions Ray Chinn says: "An upward move towards the low teens is probably where we should get to. How we will get there, and when, I am not yet sure."

Self-employment

While some choose self-employment, perhaps lucratively, as a group they are woefully underinvested in pensions. "They are a big group now and only going to get bigger," says Royal London personal finance specialist Helen Morrissey. "They are having a difficult



Terms of employment

Source: CIPD UK Working Lives – Job Quality Index 2018

time. Pension provision is actually decreasing – we are at a real crisis point. We need to make sure they are getting the support they need."

The success of auto-enrolment has led to consideration of whether the 'nudge' trick can be replicated. "The majority want to do something but don't get around to it," says Morrissey. "The self-employed are really no different – if we can bring auto-enrolment to this group we will see a lot more sign up."

Royal London and Aviva produced a report last July recommending a nudge towards a 4 per cent contribution (and 1 per cent tax relief) at the point of submitting a tax return, into an existing workplace scheme or a new one from a panel of providers.

Government proposals are expected towards the end of the year. "They need to find nudge principles that actually work," says Aegon head of pensions Kate Smith. "Government pensions policy needs to keep on top of the employment market. We don't want a growing pensions divide, with some people unable to afford to retire."

Plenty of products exist for those willing to save. "There is no reason why they couldn't go into master trusts – they are their own employer," says Equiniti propositions and solutions director Chris Connelly. "It might offer more comfort, with an extra level of governance."

The pensions dashboard, slated to go live in 2019, will help those will disparate pension pots keep track of their overall position.

The gig economy

The pensions problem is most acute in the gig economy, which covers many of the five million self-employed and includes 800,000 people on zero-hours contracts. Extending auto-enrolment to this combined group would result in an average pot of £75,000, according to Pensions Policy Institute modelling for Zurich last November.

Such arrangements legally circumvent employment rules, including auto-enrolment. "Employers stand to save a lot of money employing people under those terms," says Morrissey. "Although workers do also want increased flexibility."

The evolving legal situation is producing peculiar outcomes. For example, Uber drivers are considered employees (and are now offered some workplace benefits, including pensions advice) while Deliveroo riders are deemed self-employed. In June, the Pimlico Plumbers case ended with the ruling that a tribunal was entitled to conclude that the contractor was employed, despite being VAT registered.

The July 2017 Taylor Review into working practices made a series of proposals to bring all workers' rights onto a more even footing, which the government has promised to implement. The Independent Workers of Great Britain (IWGB) union has sprung up to protect the informal workers.

"The challenge for the market is how it can be innovative for the smaller pots," says Connelly. "There is much more innovation going on at the higher wealth end. The people who most need a bit of help, protection and advice are those that do not have so much."

Accumulation innovation

Self-employed and gig workers need products that can cope with unpredictable incomes. Locking money away is especially risky where sick pay is not provided; fear of unforeseen expenditure is a major barrier.

However, the understandably strict rules around pensions make innovation difficult. "Hybrids are difficult due to the way tax relief works, which is extremely generous for pensions," says Smith. "How could the government give the same tax incentive and allow access earlier?"

Individual Savings Accounts (ISAs) are the main alternative, which offer greater flexibility but more limited tax advantages. "It's probably better to save in a cash ISA as a rainy-day pot and a pension for longer-term saving," says Smith.

Nest is conducting a pilot scheme that combines pension and saving accounts, which it describes as a savings 'sidecar'. Money is initially saved in the sidecar, from which withdrawals are permitted, but tips it over into pension savings after reaching a certain level.

However, the sidecar is not considered an eligible auto-enrolment scheme, so it only applies to saving

beyond the minimum contribution rates and does not attract tax relief or employer contributions. It would require a change in the law – but the pensions and financial inclusion minister Guy Opperman has expressed an interest.

Chinn says it adds value in habit-forming and simplicity. "It's about getting the two working in tandem and making the journey frictionless. It's a potential support mechanism for the self-employed in the gig economy that have more pressing liquidity needs. If they go through periods where they can't work, or can't find work, liquid savings would be more important than retirement saving."

Guided investment pathways

The other major change is the disappearance of a cliff-edge retirement date. One in four people believe they will be working at 70 years old, according to Aegon.

Such practices necessitated flexible decumulation rules, embodied in the pensions freedoms of 2015. The Financial Conduct Authority (FCA) reported in June that the majority now shun annuities and opt to draw down capital when it's needed.

Pre-freedoms, schemes' final responsibility was converting (or facilitating via the open market option) the pot into an annuity. However, now there may be a series of decisions taking place long after full-time employment ends.

"Even if they do not work for the company, the member remains a liability of the scheme in every sense," says Connelly. "There is a duty of care in trust-based schemes and contractual obligations in contract-based ones until the last penny has been paid. They are responsible for making sure these people are making responsible decisions. The FCA requires it, standard trust regulations require it and the law requires it."

Many members take independent advice, perhaps with employer assistance, but many shun it (a third of which remain solely invested in cash). While initial fears of squandered pots were overdone it found insufficient competitive pressure in decumulation with charges as high as 1.6 per cent, far exceeding the 0.75 per cent accumulation charges cap.

The industry and official bodies now seem to be coalescing around a packaged approach. The FCA recommended the creation of 'investment pathways' to seamlessly provide a solution that meets members' needs – they would simply be led towards an outcome based on expressed preferences.

This could initially involve drawdown (perhaps while working part-time) followed by the purchase of an annuity for more more advanced years. "A default decumulation plan makes a lot of sense," says Connelly. Leading schemes design a customer journey framed in life choices such as a career change or phased retirement. "It leads us to increasingly doing it online," he says. "Being flexible and tailored to the member's unique circumstances is then much easier."

Smith adds: "You will find people mixing and matching, accessing their pension but also working and continuing to save in their new employer's scheme. People will be auto-enrolled even while they take some of their retirement income – they can still put away £4,000 per year."

There will be a hierarchy of demands but establishing a savings habit is important. Adds Connelly: "They need to build in a ratcheting mechanism so they save as soon as they can afford to do so. They need to recognise that it is their job to do it."

Written by Alastair O'Dell, a freelance journalist