Summary
- Freedom and choice has been popular, with a dramatic rise in the popularity of drawdown and a higher than expected level of DB transfer activity.
- The reforms have faced limitations over the past five years, notably in terms of member understanding and the accessibility of financial advice.
- Further reforms and greater protections are needed to protect members and 'future proof' the freedoms; but views on how this should be achieved differ.

Five years of freedoms

Five years on from the introduction of freedom and choice, Sophie Smith looks at what impact it has had on the industry, and what the next five years could hold

The pension freedoms celebrates its fifth birthday this month, albeit in unusual circumstances, far different from those in which they were originally introduced. Whilst in day-to-day life, many are facing increasing restrictions upon their freedoms thanks to the impact of social distancing and quarantines, the freedom and choice reforms still see savers benefit from much greater flexibility when it comes to their retirement.

"The introduction of the pension freedoms in 2014/15 revolutionised the retirement landscape," argues Association of British Insurers (ABI) head of long-term savings and assistant director, Rob Yuille. "People now have far greater choice in how to shape their retirement finances, and the policy is working well for many."

However, Yuille emphasises that despite a positive reception, and improved consumer choice, it's no surprise that the landmark policy has created challenges, especially with key limitations on its progress.

"The biggest limitation has been lack of financial education and inadequate supervision of certain advisers," says Pension Scams Industry Group (PSIG) chair, Margaret Snowdon, arguing that a broader campaign on financial education is critical to improving how members utilise the freedoms.

Agreeing, The People's Pension director of policy, Gregg McClymont, points out that the pension freedom puts the risks of decumulation on the individual, including risks around investment performance and longevity. "These are hard to manage for professionals so will be very tough to manage," he adds, "even for highly engaged savers".

Snowdon adds that whilst freedoms were a good idea philosophically, it presupposed that people would make sensible choices, emphasising that without an adequate understanding of the true consequences of their decisions, pensions freedoms can in fact be "a dangerous tool" for many members.

"A major beneficiary of the change has been the exchequer," she points out, "who has benefitted in tax take many multiples of what it forecast". This indicates how many people may have acted unwisely, she says.

The real winners

This message is echoed by Lane Clark and Peacock partner, Steve Webb, who highlights data on unexpectedly high tax revenues from the policy as evidence that it has been more widely taken up than expected, not least with regard to DB transfers. Webb emphasises, however, that the core issue lies in the support members are given while navigating their pension freedoms.

"DB schemes are taking a range of approaches to supporting members. This does mean that the level of support that members get from their scheme can be something of a lottery," he explains.

Indeed, just as the British public have turned to medical experts to guide them through the coronavirus pandemic, so too should scheme members be able to turn to financial experts. The introduction of freedoms in 2015 saw a surge in adviser demand, and Snowdon emphasises that sourcing an adviser can

be a struggle. Plus, with recent research by the Financial Conduct Authority (FCA) revealing that as much as 76 per cent of firms with DB transfer advice permission could be giving harmful advice, are members being left in 'isolation' with no support in sight?

Left in isolation?

Webb acknowledges that trustees are often very wary of getting too involved in supporting members for fear of liability should things go wrong, but emphasises that they should at least be ensuring good member take up of impartial guidance services, such as Pension Wise.

"They should also be engaging with members well before retirement," Webb recommends, "before decisions have been taken, so that members are aware of the full range of options that they have and where they can find help. Schemes should also take advice on how far it would be appropriate for them to facilitate access to financial advice, possibly at a reduced cost to the member."

However, Snowdon argues that the industry has been "hamstrung" by the "regulatory obsession" with financial advice, echoing Webb's concern that scheme trustees and managers may fear "inadvertently" providing advice.

"People want help with their decisions, and we ought to be making it easier for them to get this," Snowdon argues."We have thousands of administrators who could help if they were empowered to do so. I hope the Money and Pensions Service (Maps) will see this as a great opportunity."

Avoiding catastrophe

But whilst the industry continues to adapt to support the reforms, pension scammers have already stepped in, seeking out and targeting those members failed by the level of support and advice available from the industry.

"Freedom and choice has changed the terms of the consumer outcomes debate," Age UK senior policy manager, Chris Brooks, states. "Previously we all tried to help people shop around and get the highest annuity rate, while now that's not the main priority.

"Instead this is now about avoiding catastrophic outcomes such as scams, which is bad as we should be focusing on people getting the most from their money and enabling them to have a good standard of life throughout retirement."

The next five years

Brooks' warning that much stronger protections are essential if freedom and choice is to be a success is one often echoed by experts across the industry, with an overwhelming call for greater member support.

"There is a growing belief across industry that more needs to be done to help ensure the market works most effectively, safeguarding future savers and helping them to avoid negative outcomes," Yuille adds.

However, the route to greater member protection has less agreement, as Webb points to protections such as mandatory guidance or a rapid increase in the age of access, while Brooks states that further product pathways will be critical in ensuring members get the best experience, and value, from their pension.

"Freedom and choice users will increasingly experience cognitive decline, which will make managing their money more difficult, and the industry and regulators need to be proactive in dealing with this, or many of the oldest old could lose out significantly," he explains.

Brooks argues that all members should be defaulted into Pension Wise to encourage a greater understanding of their options, adding that this would need to be combined with the investment and, perhaps most importantly, the product side.

Equally however, whilst Snowdon points to existing industry regulators and associations such as Maps for member support, Brooks argues for an immediate taskforce to deal with the issue "before significant harm starts to emerge".

Perspective is key

"Analysing just one policy change five years ago…will not paint a full picture of the retirement landscape and how it could improve," argues Brooks, adding that not all members will have adequate savings to make use of the reforms.

"To future-proof the freedoms," he adds, "we need to look at broader pensions policy, including saving levels, and much wider, including housing and benefits."

Snowdon emphasises this, arguing that the fundamental change needed is to simplify pensions and improve the transparency of charges and returns, clarifying that this is more important than "gimmicky freedom".

The jury is still out on the success of the pension freedoms, and in a long-term game like pensions, it seems likely that we will only be able to judge the true impact on members decades from now.

Written by Sophie Smith

The impact of a quarantine birthday?

The Covid-19 outbreak has had a huge impact on pension schemes and savings, with River and Mercantile describing Covid-19 as the "perfect storm…in terms of funding" for schemes. But what is the impact on individual members, and those navigating their newfound freedom?

"The drop in the markets will harm anyone who's over-exposed in equities," Age UK senior policy manager, Chris Brooks, explains, "which could include people who recently retired and who have moved into drawdown, particularly those who didn't use an adviser". This will obviously harm them in the short term, he adds, "but could have long-term consequences too because of sequencing risk; for example, it's not possible to make up for losses experienced early in retirement".

"While it's true that lots of recent retirees still have other sources of income, it would be a big mistake to dismiss this problem altogether as many people will still lose out, and at the very least it highlights the need to prepare for a few years' time when far more people are relying on their DC savings," Brooks adds.