ROUNDTABLE

SPEAKERS PANEL

CHRIS ATKIN
Atkin Trustees

MARK FUTCHER
Barnett Waddingham

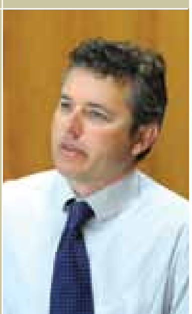
"To what extent can the state facilitate or capitalise employee-related savings?"

MICHAEL JOHNSON
Centre for Policy Studies

ANDREW WARWICK-THOMPSON
Hewitt Associates

"It is very complex to understand why people will not save"

"There is clearly an inherent interest in the individual to save"



JONATHAN WATTS-LAY
Wealth at Work

SAVINGS CULTURE

Whose job is it to make sure workers are saving for pensions?

CHARLIE THOMAS
EXECUTIVE EDITOR, Pensions Management

CHARLIE THOMAS: Who is responsible for the long-term financial well-being of employees? Should the government be doing more to encourage employers to provide workplace savings, and to what extent can the two interact without stepping on each other's toes?

JONATHAN WATTS-LAY: My view is it's a shared responsibility. There is clearly an inherent interest in the individual to save, because it is about the lifestyle that ultimately they are going to have, whether at retirement or before.

Also, even though the pension onus has swung away from the employer to the employee, there is a balance that has to be struck, because if the employers are not at least making their employees aware of the issues they may face come retirement, there is a consequence ultimately for those organisations.

MARK FUTCHER: With the shift from defined benefit (DB) to defined contribution (DC) pensions, there has been a change of emphasis from the employer taking responsibility for risk management and providing decent pensions to the individual.

Individuals need to start taking more responsibility for themselves, but having the tools to do that is key. Many of the employers that we engage with do not want to just comply with the bare minimum; they want to do more for their employees.

We all know why people do not like pensions. There is a lot of bad press about them. They are inaccessible. Companies are recognising that and want to address short and medium-term savings and debt management.

ANDREW WARWICK-THOMPSON: It's a fundamental issue of workforce management. One of the things that worries HR directors about the removal of the compulsory retirement age is that you cannot plan talent renewal. The other worry is [the employees] do not have enough money to retire on.

Most of the big employers we talk to who take talent management seriously can see the provision of generous retirement benefits, whether that is provided through ISAs or DC or DB plans, is an important part of their role as is encouraging people to make provision for themselves.

It is probably less costly in the long

run to make sure people are able to retire in comfort than it is to have them stuck on the payroll for donkeys' years because you cannot retire them.

CHRIS ATKIN: Do you see employers with this problem of how to get rid of older employees now?

WARWICK-THOMPSON: They call it talent management.

ATKIN: Will employers look at ways of targeting their resources into making provision for the employees they want to get rid of at perhaps an earlier age?

WARWICK-THOMPSON: They used to do it through DB plans, but now it has to be done on the profit and loss sheet.

ATKIN: Employees are responsible for their own wellbeing and retirement. The employer is a facilitator. Good employers should recognise they are doing something more in this area, but it should not be compulsory that they do it. Rather, the employee should take responsibility for themselves.

WARWICK-THOMPSON: Ultimately, the employer is going to pay for it. It does not matter whether they pay for it through redundancy, through pensions or some other means.

JOHNSON: I do not agree with that. Ultimately, it's the taxpayer who pays for it, to the extent that we have people coming out of work with insufficient savings or pension provision [who then] fall back on the state.

The question perhaps is easier to answer by saying who is not responsible and I think the employer is not responsible at all. The dilemma here is it's the government that carries the can, but to what extent is there a role for government to be involved? The National Employment Savings Trust (Nest) is a little hint.

THOMAS: The short-term nature of government surely makes it impossible for any government to set up any long-term plans?

JOHNSON: That is a perennial problem, but there are some wise heads in government who realise that position is no longer sustainable. The question is, to what extent the state can facilitate or catalyse employee-related savings? There is an opportunity to harness the employer/employee relationship; the former is effectively a distribution agent and I can see that role becoming more significant in the future with incentives from government. Nest is the start of that.

WARWICK-THOMPSON: I am not sure I agree with that, but that may be due to the nature of the employers we talk to. I can see that Nest works for the vast number of small businesses, but Nest is irrelevant for the larger businesses.

THOMAS: A number of insurers are looking into producing an alternative to Nest and they are marketing it as such.

WARWICK-THOMPSON: Absolutely. There are already employers who are going to be looking for alternatives. They feel it is their responsibility to provide something better or at least equivalent to Nest, which is to brand it themselves.

"The big employers can probably afford the resources to offer a full range of advice and education, but smaller employers cannot"

JOHNSON: How many are going to level down, post-Nest, the employer contribution?

FUTCHER: The Association of Consulting Actuaries said 41% recently.

JOHNSON: The temptation is going to be enormous.

WATTS-LAY: There are two things that come out of this. One is responsibility versus accountability and what you are talking about is government accountability, not responsibility.

The second point regarding where money is spent is there are a lot of employers saying, "We spend 10% per head of base salary on pensions at the moment, but they do not engage employees."

More employers are going to their employees and saying: "Here is the 10%, you decide how you want to spend it. We do not really care anymore if you spend it on pensions or not." For them, it is about the engagement of their employees and how they are going to recruit and retain the staff they want.

THOMAS: Have you seen any change in the paternalistic attitudes of employers over the last 10 to 15 years?

ATKIN: Within the DB forum, basically every employer wants to get out of it. Many employers would like to get shot of it tomorrow.

On the DC side, the big employers can probably afford the resources to offer a full range of advice and education, but smaller employers cannot. I think many companies will just reduce their pension advice down to the basic minimum.

FUTCHER: There is no clear strategy from government. It has changed its mind so many times over the past 10 years; we have not been able to get a clear strategy for your planning needs. I think probably everyone thinks auto-enrolment is a good idea, but wrapping it up in Nest is adding complications.

JOHNSON: The Treasury hates Nest's cost implications, and consequently some internal tension may become evident in the next two months. There is the government view and there is the Cameron view. If one goes back to his philosophy document, which sets out the way he thinks, called *Built to last*, it is all about personal responsibility. Therefore, I think if one was to ask him rather than Steve Webb – let us not forget the coalition angle to this – he would say it is down to the individual.

WARWICK-THOMPSON: Personal responsibility will only work if you remove the safety net. Going back to your point earlier, ultimately the government is the insurer of last resort. If you bring people up to believe that at some point if anything goes wrong the nanny state will step in and look after them –

JOHNSON: Do people really believe that, though?

WARWICK-THOMPSON: It is very complex to understand why people will not save. One reason is they mistrust pensions, because there has been a lot of bad publicity about pensions being a rip-off. Younger people do not invest in pensions because they do not like the idea of tying their money up long term. I am not convinced that by merely introducing ISAs into the workplace for shorter-term savings will encourage employees to save more.

FUTCHER: ISAs are one product that has worked in the UK. They are very simple. There is something like £275bn in ISAs.

WARWICK-THOMPSON: Most of it is in cash, though.

WATTS-LAY: It would be in the workplace as well. The 25-year-old has more worries about potentially paying off debt, and they want to buy a house or a car. A pension is not a priority. It comes back to "What benefits are we going to offer as a company that are going to be attractive to this person?" If they can offer attractive shorter-term savings at the cost or the expense of not paying into the pension, not forever but for a few years, then maybe that is a good thing to do.

Getting people into a cultural habit of saving, whether it is for the short or long term – but based on the needs that they have – which drives engagement, is the key.

THOMAS: Another key point is the fluidity of young people's work now. Nobody at 25 expects to be in the same company in 20 years' time, which is a key reason why they do not bother joining things like share-save schemes and pension schemes; they do not expect to be there longer than 18 months and they are not portable.

ATKIN: Whereas group ISAs could be. Do you want to tie your money up, as a 25-year-old, for the next 30 years when you can only get it out in dribs and drabs if you live to 100? Is that really a sensible investment? I have to say no, it is not.

WARWICK-THOMPSON: We still have plenty of employers who have put in things such as share plans, who have started to put in ISAs and the take-up rate is not that high. You can put money on the table and people do not take it up. We've seen non-contributory schemes people have not joined. Auto-enrolment may or may not make much change, because people can opt out of it if they want to.

WATTS-LAY: You are right. Staff are not educated about those benefits. A pension pack is given on the first week of employment, but that individual probably has a lot more to think about in their first week of employment than worrying about the pension. There will be the annual email that comes out from the pensions department and a few other bits and pieces, which they will probably never read or, if they do read it, the chances are they will not really understand it and it never gets started.

The key issue is people have to have good education in the workplace to understand what the benefits are to make informed judgements.

ATKIN: Why are you saying in the workplace? Why is the employer obliged?

WATTS-LAY: If they do not believe it will help them commercially they should not offer the benefits, full stop. Presumably, therefore, they are only offering it because they believe it will help. If they do not believe it will help, they should not offer it.

ATKIN: That has often been the irony of pension schemes: you poured tonnes of money into a pension scheme and the employees have not appreciated it.

JOHNSON: Financial education is an alternative to regulation.

WATTS-LAY: I would not say that. When you get into the regulatory bit, you open up a real can of worms. Since the legislation around workplace benefits is different from the retail market, there is a complete mismatch there. If you were to go and see an IFA as an individual and said: "I am 30 years of age, I want to buy a flat, I want to do this, I want to do that", you are very unlikely to be offered the type of structured benefit that many people are offered on day one in the workplace. That is, that IFA, under the suitability rules, would not be allowed to say: "I tell you what, buy a pension." That is part of the issue.

JOHNSON: One option is to highly educate everyone financially so they make wise decisions and then they will essentially eschew the financial-services industry. They will realise that the complexity is by and large smoke and mirrors.

"Younger people do not invest in pensions because they do not like the idea of tying their money up long term"

Alternatively, one can go down the strict regulatory framework and, for example, compel saving. That is an extreme form of regulation and it is nothing to do with financial education, but it might meet the government's objective of in 30 or 40 years' time the government not having to pick up the tab. Inevitably, therefore, over the next few years – the compulsion word is going to enter the lexicon more frequently.

The issue here is, if we think about generation Y – the under-35s – it is not so much trying to persuade them to save within a pension framework, it is trying to persuade them to save at all. I am strongly in favour of ISAs being included in auto-enrolment because I think they'll help kick-start this.

WARWICK-THOMPSON: Why pussyfoot around with ISAs, though? Why not just make it compulsory to save?

JOHNSON: Pensions are a bad investment.

WARWICK-THOMPSON: Why?

JOHNSON: Let us take the Treasury's perspective for a second. It provides 40% tax relief for higher-rate taxpayers. Only one in seven higher-rate taxpayers while

working is going to subsequently repay the Treasury at 40%. Therefore, from the Treasury's perspective, it is an abysmal investment.

WARWICK-THOMPSON: If you make pensions compulsory, why do you need to have any tax relief at all?

JOHNSON: You do not. I would be in favour of getting rid of it all.

WARWICK-THOMPSON: Fine, so you get rid of tax relief, you make savings in some sort of company pension scheme or in Nest, you make it compulsory, you remove all of the tax breaks, because the tax break is only there as an incentive. We are not incentivising people because we are making it compulsory.

Why mess around talking about education, why try to get people into the savings habit? Just make it compulsory, remove the tax breaks and get on with it.

JOHNSON: Yes, but there is one little detail that you are forgetting which is absolutely crucial; governments like to be re-elected.

WARWICK-THOMPSON: Which goes to Charlie's point about whether you can get a sensible decision out of someone who is going to be looking for re-election in five years' time.

FUTCHER: It has to be a long-term view and it cannot change every five or 10 years. That is the problem. That is all employers are talking about.

JOHNSON: If we look at the history of the introduction of compulsory savings, everyone jumps up and talks about Australia, which is a complete red herring.

Employees in Australia are not compelled to do anything. The compulsion is purely on the employer. The only countries that have ever successfully introduced compulsory employee saving have, at that time, been run by right-wing dictatorships.

FUTCHER: On the education point, though, pensions are getting a bad press at the moment. The big reason for that is people are living far too long or much longer than they were.

ATKIN: They are not living too long; they are not working long enough.

FUTCHER: Okay, but the problem is the gap between when they retire and when they are reliant on their pension has grown from three years when pensions were first introduced up to 30 years.

People are only paying into pensions or savings for the same amount of time as they expect to draw them and that cannot be right. Putting in

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10% of salary or 20% of salary is not going to provide 66% of salary by the time they retire.

ATKIN: I don't worry about the under-35 generation, they have a different lifestyle, a different attitude to work. They can change jobs a lot more than my generation could or did. They will take a year out to go and travel and do things.

The 65-year-olds are still under the old system and it all works reasonably well. It is the generation of 40-55 who are the difficult generation to cope with, because they have an expectation of what went before, which is unaffordable, and they have not moved into the different lifestyle. That is the generation that we need to sort out and it is a shorter-term issue.

THOMAS: So should financial education be focused on that lost generation of 40 to 55-year-olds?

WATTS-LAY: Yes, and I think they are. We have educated 24,000 people in the UK in the workplace in the last four years and I have absolute empirical evidence as to how it works.

WARWICK-THOMPSON: Communication does not work, but I think education and advice does.

JOHNSON: While 24,000 is admirable, but what about the other 30 million? It seems an unfair division of labour to spend huge amounts of time, energy and money educating people to a level where you hope they are going to look after their finances.

WATTS-LAY: The only reason a company should be offering a benefit is because they believe it drives some commercial benefit for them. If they do not believe that, they should just get rid of it. Therefore, on the basic principle they are only providing the benefit because of that, how do you maximise the value?

Some of the more recent changes, such as share schemes to pension and driving double tax relief and all those sorts of things, particularly in hard times it is a way to drive more value for their employees but at no extra cost to them.

WARWICK-THOMPSON: Therefore, financial education needs to start with the employer, to demonstrate to the employer there is a long-term business advantage to providing benefits and providing the education. Educating employees is secondary to that.

WATTS-LAY: Ten years ago when a lot of DB schemes were closing and DC was coming in, a lot of pension managers and reward directors knew it was not as good as the DB and said: "We will just implement it and try not to talk too much about it." Ten years on, people have come through the other side and companies are saying: "What we now have to do is make sure that we maximise value for our employees, because we want to recruit the best people, retain the best people."

THOMAS: Is advice being provided properly in the workplace and, if not, who should be providing it?

ATKIN: The concentration of financial advice tends to be at retirement. That is where it comes in. It is based on "this is what you have, what is the best way to deal with what you have?" It is greatly appreciated by the people who receive it, if they receive financial advice, because they just need some guidance as to how best to plan the rest of their lives.

Certainly in smaller schemes, that advice sometimes doesn't happen.

JOHNSON: Many people simply

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want to be told what to do. Choice is part of this equation and choice is a wonderful libertarian ideal, but it is counter-productive in this context.

FUTCHER: People have to understand the choice they are going to make and I think there is a very fine line between education and advice. When you give education you are probably, in the Financial Services Authority's rulebook, dancing all over the line of advice.

I do lots of presentations. We go into factories, and people have come up afterwards and said: "I have never understood what a pension is. It is just a glorified savings account, is it not?" That is exactly right.

JOHNSON: But you cannot get access to it for 25 or 35 years and there is an uncertain, distant return.

FUTCHER: That is what people like about pensions, because people cannot trust themselves to save. People who save up go: "I have £5,000 or £6,000 in my ISA now. I am going to take it out and I am going to buy a new car, I am going to buy a plasma TV, I am going to go on holiday". The good thing about pensions is that you cannot get access to money.

JOHNSON: But that is a huge barrier to getting people to start.

WARWICK-THOMPSON: Which is why you make it compulsory.

THOMAS: Is anyone concerned that in 2012, with nine million people being forced into a pension for the first time, regardless of whether they opt out two weeks later or not, that the advice issue hasn't been addressed?

If everyone has these presentations, are you confident that the public will understand exactly what options are available to them and be able to make a choice?

WARWICK-THOMPSON: That is what companies that employ consultants do, but going to Michael's point, what about those companies that cannot afford or do not have the option to do any education? Their employees will just end up in Nest.

FUTCHER: There is no education; that is the point.

THOMAS: Agreed. There is no education or advice planned or communication about Nest and what it means for those lower earners who do not have employers who can afford to have a scheme.

FUTCHER: The low earners are the ones we have spoken to. They sit on a factory line. They have worked all their lives. They have worked from 16 and they are more than happy to work to 65, 70, whenever. They have been earning £12,000 from their employer, they put a little bit aside into a pension scheme. They are going to retire on a state pension of £7,000 or £8,000, plus they have a little bit of money tucked away in their private pension pot. So, they earn £12,000 a year while working and retire on £10,000; that is not the problem group for me, it is the next group up. Those earning between £15,000 and, say, £45,000, are the biggest problem. They are used to a higher standard of living and yet they are still not putting much money away.

ATKIN: Picking up your point that you are going to have nine million people putting money in, building up small pots, maybe reaching £20,000 or £30,000 eventually. They are not going to be interested in playing with or investing that. They will just put it into a default bond and forget about it. I have heard of fairly reasonably sized earners who maybe put 10% into a pension scheme every year and have no idea where it's invested, and they are happy with that.

WARWICK-THOMPSON: The question is who sets the default. You are coming at it from a trustee's perspective, so I can feel comfortable because I know that Atkin Trustees, for instance, is looking after my interests in some way. They have chosen a sensible default strategy, may have taken some advice, and almost make the decision for me.

What if I am in the increasing proportion of employers who are going down the deferred self-invested personal pension route? We have some very big ones, such as BP, BT, who are in that category.

Where is the decision being made then? Whose responsibility is it then? You either come back to the individual having to make decisions, which brings you back to the education issue, or that it is the employer's responsibility to make sure that there is something sensible in place.

JOHNSON: There is a third route, which is a strategy I favour for Nest, which is to turn Nest into a sovereign wealth fund and compel particularly the public sector to participate. Essentially, over a relatively short time frame, we would build up an enormous with-profits fund, in essence, in a number of silos.

Ultimately, the question about who makes the decisions about asset allocation would rest with all

> **"Choice is a wonderful libertarian ideal, but I think it is counter-productive in this context"**

the private-sector contractors managing the assets. You cannot leave it with the employee because they lack the education and wherewithal or interest and you cannot leave it with the employer. Inevitably, therefore, it falls back again onto the state, which should sub-contract the responsibility to the private sector.

Given the state is the one that picks up the can, it is in the state's interest to pay all the costs to encourage mass participation, including the 30 basis points a year and 2% subscription fee that is currently being talked about. That should be picked up by the state, because unless we catalyse an avalanche of savings over the next 15-20 years, we are going to have a major fiscal problem.

THOMAS: To encourage engagement and participation with pension products, is it better to pitch them on an individual basis, or can you present them company-wide for all these mass corporates?

WATTS-LAY: In the main, companies are looking at having some core product offerings that are company-wide, but maybe specific subsets within that; the employer-financed retirement benefit scheme is probably a good example of one that is quoted quite a lot at the moment. However, I think the whole notion is one of giving employees an element of choice and then explaining the pros and cons of these choices.

One of the key things is that it is not a decision you make on day one and then live with for the rest of the time you are in that company. To maximise value as an employee, and to have maximum value from the employer perspective, you need this notion of annual windows for savings vehicles, the same as for traditional flexible benefits.

THOMAS: Have the advances in technology helped to make it more accessible?

WATTS-LAY: Yes, definitely.

ATKIN: But I think that is dangerous ground for the employer to start presenting the pros and cons of things. On complex benefits you do not go into the pros and cons if you are incorporating savings products or financial products into your flexible benefits package effectively.

WARWICK-THOMPSON: Yes, but this tends to get foisted onto the employer.

WATTS-LAY: A lot of companies now ask: "What can we offer our staff as short-term savings?" They might say ISAs are relatively short term, save-as-you-earn schemes are relatively short term. "What can we offer them as medium-term savings options?" That might be longer-term share incentive plans, things of that nature. "What can we offer them as long term?" That would typically be the pension.

If all things were equal, you would put one-third, one-third, one-third, would you not? However, people will make judgements. People have personal situations where the individual says: "Well, I am 25 and what I really care about is saving for a flat." Therefore, they will understand the pros and cons of going down the shorter-term route than the long-term route.

JOHNSON: Well, the statistics for ISAs, which one would assume to be a short-term product in this context, illustrate remarkable persistency. The people who started off with PEPs, and subsequently ISAs, put a few grand away each year, year after year, and what one ends up with is a long-term savings scheme, so it is not a short-term product.

WATTS-LAY: Yes, but it gives them the ability to use it short term.

JOHNSON: The reality that emerges is different, though – and that is the problem.

WATTS-LAY: That is not a problem; it is a benefit.

JOHNSON: There is a disconnect between behaviour and product offering.

WATTS-LAY: That is the benefit, not the problem. The benefit is that you encourage people to save. If it turns into long-term saving, great, because that was the objective.

FUTCHER: The only way the government can increase workplace savings is to make it compulsory, but lots of companies are not going to understand the argument that it drives the bottom line.

JOHNSON: There are a number of proposals, some of which the industry is going to hate.

I am an advocate of some form of compulsory saving in an amended Nest structure, not linked to employment status, where all the costs are picked up by the state so the individual and the state can benefit from the power of compounding over the individual's working lifetime.

Otherwise the state will pick up the bill anyway and that individual falls back into the means-tested trap when they reach 55, 60, 65. Inevitably, when one has these conversations with people in the industry, we do not face up to the fact that the industry is overpaid, charges are ludicrously high.

FUTCHER: As an aside on the compounding of charges. Nest will have a 2% charge upfront, plus a 0.3% annual management charge.

JOHNSON: That is insane. It's a huge deterrent to participation.

WARWICK-THOMPSON: Ah, yes, well, they have to pay Tata somehow. The government was not going to pay, so they have had to come up with a contribution deduction structure.

FUTCHER: One thing that we have not mentioned, which I think is very important and we have done a lot of work on, is behavioural finance and behavioural challenges. I reckon there are six main things that stop employees saving: the top one being they are skint.

But workplace savings get around a lot of the problems, because if my employer said to me: "I have an ISA here, it is low charged – probably not the lowest charged, but it is very simple – we collect your money from your pay and we pay it across", that removes a massive barrier from most people saving.

THOMAS: Does anybody think workplace savings will not increase over the next two years, five years, 10 years? If so, why?

WARWICK-THOMPSON: It will increase, but to Michael's point, it probably is not going to generate

"The only way the government can increase workplace savings is to make it compulsory"

the trillions that you need to resolve the problem. It will help, but it will only scratch the surface.

FUTCHER: There is no golden bullet, is there? That is the problem.

JOHNSON: You asked the question why – fear is quite a strong motive and we will see over the next 10, 15, 20 years real pensioner poverty, which will be in the media and will incentivise people not to get themselves in that position. I think the fear factor should not be underestimated.

WARWICK-THOMPSON: How long will it take for that to take effect? When do we see our first starving pensioners? When does that hit the headlines?

JOHNSON: I think that is probably too extreme and hopefully we will never see that.

WARWICK-THOMPSON: Is that not what is needed, though? Do you not need to see starving people on your TV screen before it has an impact? It is all part of education, is it not, to scare people to death?

JOHNSON: There is a lot of evidence of the power of fear already and that is simply if one graphs economic growth or GDP and on the same graph puts the household savings ratio, there is a very strong correlation that the savings ratio goes up when GDP goes down. PM