

xafinity paymaster 



## Building personal accounts: securing a retirement income

Xafinity Paymaster's response, March 2009

# Building personal accounts: securing a retirement income

We are delighted to have contributed to the consultation on securing a retirement income. Our consultation response is based on our extensive experience in pension administration and the provision of annuity administration services.

Our answers seek to balance the aim to keep the cost of administration low with the aim to meet member needs. This balancing act is something we understand very well.

In our response we have made the following key recommendations:

- A wider communications exercise is needed to educate the public on the process of converting savings into a retirement income.
- Against the backdrop of increased awareness, the scheme should communicate with members from the age of 55 in order to get members to start thinking about their options, using the internet and other appropriate low cost channels.
- There is no reason to assume that members will want to convert their savings into a retirement income at State Pension Age. With the likelihood of more flexible retirement working patterns, this is not necessarily going to be the norm.
- At age 75 there should be a default approach for those members who still have a pot, though the issue is likely to be tracking down these members.

We also draw your attention to the following points which we are happy to discuss in more detail if that is helpful:

- However much the choices are simplified people still find the choice bewildering. If there is a phone channel available people will use it rather than the internet.
- There may need to be a backstop in case the panel approach does not work.
- We are unclear whether the scheme administrator will have the correct date of birth for all members and if not this will be a problem.
- We believe there is a good solution to making payments to the 'un-banked', which is pre-paid cards.
- We see no issues with paying overseas. The main issue is likely to be tracing the non-UK members.

A summary of our response to the consultation questions is given on the following pages.



## Are lifetime annuities the best way to provide a guaranteed lifetime income for our members?

- Within the current statutory environment they are the only way to provide a guaranteed lifetime income for members.

## Does our research into the way our target market views the process of buying annuities reflect your own views and experience? What other factors do we need to consider that will help us better understand our audience?

- Yes. The purchase of an annuity is a complex process for many members of arrangements based upon a defined contribution form of pension provision. There is still a reluctance to seek the advice of IFAs and despite numerous initiatives the OMO is still rarely taken up.

## Are the levels of choice we are offering to enable members to buy annuities the right ones? Should we be offering others?

- Even with a focused choice option we think that most members in the target market will still find this bewildering.
- We do not recommend offering further choices.

## What could the personal accounts scheme do to minimise enquiries from employees to employers about the process of securing a retirement income?

- How scheme communication is handled will be vital in determining how the member behaves. Making members want to take greater ownership and feel that it is their own responsibility, will minimise employer contact where that employer seeks minimal involvement.
- The extent to which members will contact their employer rather than the scheme to discuss options for converting their savings into a retirement income will depend on whether they connect the scheme with their

employer or not and the perception of the level of support they are likely to get from their employer vs the perception of the level of support from the scheme.

- Enquiries to employers will be reduced if there is widespread advice available from other sources. Could the money guidance provisions or Citizens Advice Bureaux provide support to help people make the choice? It is worth considering granting all employees a day off work or two half days in order for them to consider the options (like pre-natal appointments).
- Wider public awareness of annuities and the different options would also help, as would better terminology. The word annuity does not strike a chord with the general public as the word has no natural link to the critical function it plays i.e. providing a retirement income.

## Have we identified the right type of information to give to scheme members, and are we providing this at the right points in the process?

- We see a need for radical thinking to get planning for retirement into the psyche of the public. If this is achieved, annuity selection will be straight-forward for most members.
- From the age of 55, communications with members should start preparing them for the decision on converting their savings into a retirement income. Given the vision of PADA, that the scheme should be 'more Amazon than WH Smith', we would expect such communications to be delivered via the internet but we will need to confront the issue that members may not, therefore, access this information at all.
- We are concerned that the administrator may not have the correct date of birth for all members. Unless it is mandatory for employers to provide and verify the jobholder's date of birth at the time of registration or the scheme has access to e.g. the NI database, then it is likely that the scheme will not have this data for all members. In this case a decision will need to be made about



how/when retirement income options are handled for these members.

- Other areas to address are the issues of wet signature requirements, the level of paper documentation currently required and evidencing of the member's identity. Possible easements may be needed in certain areas of regulation, which we would welcome, allowing a lot of these issues to be addressed via web based solutions.

### **To what extent have we identified the key components, and key questions, that will need to underpin our processes for helping members access retirement income products?**

- The list of key components and questions is comprehensive though it is likely to be confusing to many members and we believe that members will struggle to make a decision on their own.
- Members will have many ranges of financial awareness and it is important that there is drill-down from simplified information to more detailed technical information on options.

### **Given the objective of delivering low-cost products that are easy to arrange, are there other types of annuity products we should be considering via the panel of providers?**

- Not at this stage.

### **How can we identify the numbers and groups of people who will need alternative communication channels to using the internet? What alternatives may be appropriate?**

- We anticipate that if a phone channel is available a significant number of members will prefer to use this channel to discuss options.
- This is certainly the case in Sweden, with the PPM scheme with c.6M members. Whereas over 95% of general enquiries are made via the internet, the

majority of members reaching retirement age call to discuss their retirement income options as they find it hard to make the decision without discussing it.

- There is a need for focused research on the propensity to use the internet across demographics at key stages of the retirement process. Current research has been focused on understanding about annuities, not communication channels. It would be valid to ask the views of people in the younger age ranges. The scheme needs to deal with current attitudes and approaches but at the same time prepare itself for the near term where attitudes are likely to change.
- There is also a need to influence behaviour. Appropriate education and awareness would make people more comfortable buying annuities over the internet. Lessons could be learned from other good examples where the internet is widely used e.g. car insurance.

### **What technological innovations are likely to make internet transactions more attractive?**

- Improvements in technology and regulation which allow member data to be shared at the right times with annuity providers to avoid the lengthy and needless delays in setting up an annuity.
- Online annuity comparison tools making annuity selection as easy as buying home insurance or car insurance over the internet.
- Auto payment of tax free cash direct to the designated receiving bank accounts in parallel with straight through processing to enable the annuity to be set up immediately using electronically transmitted member data.
- Overall though, the impact of technological innovations will be limited until we see the effects of long term exposure of members to financial education/communication.



## What views do you have on the potential to use other electronic media, such as digital TV, in helping members choose annuities?

As the purchase of an annuity is a one off, irreversible decision which will have an impact on the rest of the member's (retired) life, we feel that members will generally feel happier when they can discuss such decisions with other people and get expert advice. Some things to consider are:

- Could Web 2.0 (forums and other on-line interactions) help?
- Could Expert Systems, or other AI solutions, provide expert advice and what are the legal implications of this?
- Could technology be used to gather data and preferences so that the personal interaction that does take place is as efficient and effective as possible?

## What are your views on our proposal for the trustee to buy an annuity for members who reach age 75 and don't get around to choosing an annuity?

- It is our experience that where members of a pension scheme are aware they have a benefit they will engage to ensure they receive this benefit. The issue is more likely to be tracking down members to inform them of their benefit rather than members not bothering.
- For members who have reached 75 and not made a decision and with less than £2,000 it would seem sensible, as a default approach, to contact them requesting bank account details to pay their savings as cash.
- For members who have reached 75 and not made a decision and with more than £2,000 we recommend a 'default annuity' which would need to be a single life annuity as the scheme would not necessarily be aware of whether the member is married or in a civil

partnership. A decision would have to be taken as to whether this would be an increasing or level annuity.

- This approach is best aligned with the low-cost objective of the scheme.
- The issue associated with such a default approach would be around the perception that this is a recommendation and endorsement by PADA which will need to be carefully thought through.
- It is likely, though, that the scheme will not have enough information to make these arrangements for a significant number of members (e.g. bank account details to pay into).
- When all other efforts have failed and after an elapsed period of time a final option is to use the funds to benefit the wider membership.
- It would be worth considering undertaking research as to how many members over the age of 75 there are across all pension sectors with unclaimed pension rights.

## What good practice can you share regarding how to deal with making payments to members who have not provided bank account details?

- We are working with our clients to eliminate cheque payments due to the expense and security issues. For clients with members who do not have bank accounts we can provide a pre-paid card facility. The card can be issued to members and benefits loaded onto this card at regular intervals (e.g. monthly for an annuity). Such a facility can be issued at no initial charge and without attracting transaction charges when used in retail outlets and for the withdrawal of cash once a month (subsequent withdrawals attract charges). This is therefore better than a cheque payment for the member and has none of the expense of mailing associated with regular cheque payments so helps contain the cost of administration.



## How should we address any issues raised by the need to support non-UK residents through the process of securing a retirement income?

- Facilities to make payments to non-UK members will not be an issue. We make payment to almost 200 countries in local currency.
- The issue is likely to be tracking down the member. Once tracked down, the same process as for UK residents should apply.
- For non-UK residents there is the issue of the cost of currency conversion. We would recommend that the cost should be borne by the member as is the standard approach in our experience.

## What factors do we need to consider to ensure that the panel of providers approach works effectively?

- There must be enough providers to ensure that the rates are competitive but not too many resulting in a great spread of business that makes the volumes unattractive, particularly in the early years when pots are likely to be small.
- We fully endorse your view that it is vital there is a consistent approach across all panel members to the application of funds, guarantee periods, approach to fund mismatches between quotation and acceptance stage, late arrival of documents etc. This is not currently the case in the market.
- The lower limit needs to be made clear to panel providers as it may not necessarily be £2,000. Members with pots of £2,000 or less may not take a lump sum and the effect of the pension commencement lump sum entitlement may mean that there are lower amounts.

## How should panel members be selected? Should it be by invitation only or should potential panel members be given the opportunity to bid, or register interest?

- The business and product criteria laid down are sound. Experience and proven ability in handling a mature population is fundamental. The selection should be driven by getting the most favourable all round deal and experience for the member.
- Providers must remain highly competitive in rate terms and commit to be so for a 12 month period. This also gives them a chance to manage their capital requirements and to manage their administration and delivery mechanisms.
- Rate comparisons and independent surveys of member experience and satisfaction will be a good gauge of competitiveness of the panel.

## How frequently should the membership of the panel be reviewed?

- If the criteria for selection/inclusion are effective then the frequency of review is less critical.

## What technologies are available or are being developed that would facilitate the interface between the personal accounts scheme and providers?

- The transfer of information between insurance companies/pension funds and annuity providers is becoming a more automated process. Unfortunately the amount of time required to transfer funds is too long largely due to a lack of focus and effort “to pay money away”, as well as inconsistent approaches within insurance companies and pension funds. We would suggest that the personal accounts scheme needs to work closely with the annuity providers to develop not only consistent interfaces for the transfer of information but also an agreed means of transferring and receiving funds within a short timeframe. Our corporate efforts to introduce a BACS type solution to address this issue



has met with much vocal but little commercial support. However we do feel that this has a major role to play in ensuring that the member receives his/her annuity promptly.

- In addition, our comments above regarding the easements of regulation around physical issuing and sight of documents and the requirement for wet signatures are relevant here.

#### **What alternatives to the panel of providers model should we consider to address these issues?**

- If the commutation amounts are increased significantly then it may not be necessary to form a panel as there should be a natural supply of providers via OMO.
- Otherwise, we support the panel of providers approach as it has been decided that the scheme will not be a direct provider of annuities.

#### **Have we identified all the issues that affect personal accounts scheme holders who have small pension funds?**

- Yes

#### **Do we need to consider further arrangements to rescue stranded funds, or should we be confident that the market will absorb them?**

- We feel that it is a big expectation that providers will pick up small pots as there has been very little desire shown in our experience to date.
- Increasing the commutation limit should be considered.

#### **What other approaches should we consider to resolving issues outlined in this chapter?**

- If commutation limits are not increased in order to address potential issues with supply via the panel approach it would be worth investigating an approach of moving small amounts into another vehicle such as a PISA (Pensions ISA). Sums accumulated are likely to be similar to cash ISA amounts and there are many companies which are used to managing these small funds in both administrative and investment terms. Clearly different rules regarding encashment would be required compared to cash ISAs but a requirement to hold the vehicle for a fixed term of 5 years could be appropriate.

## Conclusion

There is a need to balance the aims of minimising scheme administration with meeting member needs and this balancing act will be particularly difficult when it comes to accessing savings in retirement, as despite all the best efforts, members are likely to be bewildered by the choices they need to make. The solution lies in a wider approach to education and pragmatic scheme rules and design.

For more information on any aspect of this paper please contact [clare.ward@xafinity.com](mailto:clare.ward@xafinity.com)



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## Xafinity paymaster

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