ASSOCIATION OF CONSULTING ACTUARIES

Association of Consulting Actuaries Limited · First Floor (129) · 40 Gracechurch Street · London · EC3V 0BT
Tel: +44 (0)20 3102 6761 · Email: acahelp@aca.org.uk · Web: www.aca.org.uk

Intergenerational Project
Strategy and Competition Division
Financial Conduct Authority
12 Endeavour Square
London
E20 1JN

Via email to: dp19-02@fca.org.uk

To whom it may concern

Intergenerational Differences

We are writing on behalf of the Association of Consulting Actuaries (ACA) in response to your important Discussion Paper on Intergenerational Differences (DP19/2).

It seems clear from the Discussion Paper and our own work in this area that there are many challenges being faced by younger generations. In particular, we believe these arise from competing savings needs and greater responsibility for decision making at younger ages.

Given our practice area we have focussed many of our responses on the area of pensions. However, many of these concerns are inherently interlinked, especially in relation to saving for housing, and we have commented more broadly where appropriate.

We believe that addressing these challenges will require significant additional flexibility in the savings products that are available. For example, one option that we support is the development, with appropriate safeguards, of products that combine the ability to save efficiently for a pension (with ability to benefit from tax relief and employer contributions) with the ability to save to buy a house without incurring any penalty for withdrawing funds from the pension early.

We hope these comments are of interest and we would be happy to expand or clarify if this would be helpful.

Yours faithfully

Steven Taylor
Chintan Gandhi
Thomas Dalton

On behalf of the Association of Consulting Actuaries Limited

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APPENDIX 1

1. Are there other factors driving changes in the consumer needs of different generations (in addition to those we have listed in Chapter 3 of this paper) that we should consider? What are these?

2. Are there other ways in which the factors we have identified as driving changes influence how individuals from across different age groups build up and access wealth?

In response to Q1 and Q2, we believe the factors listed are the key factors to consider. One additional factor is the shift from Defined Benefit (DB) to Defined Contribution (DC) pensions as the primary means of retirement provision in the private sector.

From a pensions perspective this has significantly changed who is responsible for and bears the risk for meeting the needs of consumers. Consumers themselves now have much greater responsibility than in the past when employers took most pensions decisions (such as around contribution rates and investments choices) and bore most of the risk during the accumulation phase.

In combination with other complex savings challenges, we believe this results in a much greater need for support for consumers, both in terms of the products available and the guidance and advice around them.

Of particular concern for younger generations is the need to save separately for competing savings needs, such as for retirement and house purchases. For many this risks resulting in insufficient savings being directed in any individual savings area or for one area to crowd out resources for another.

For example, on page 47 of the consultation you present a largely linear set of savings challenges for young people, suggesting that a typical Millennial might purchase a house in their early thirties and that “once they have managed to buy their first property, they might want to start accumulating some form of pensions wealth”.

For many, this is unrealistic, and we believe hits the nub of the changing consumer needs as they go about building up their wealth. For example:

- under Automatic Enrolment, the majority of young people save for a pension from an early age, and many will devote significant additional resources (above the minimum combined contribution level of 8% of earnings) in order to benefit from matching employer contributions;

- under current legislation, house deposits (which have traditionally attracted significant initial savings focus for young people) must be saved for largely separately (as Lifetime ISAs cannot be used for automatic enrolment purposes); and

- when looking to take out a mortgage, lenders often determine affordability by assessing net income. Pension contributions therefore compete with consumers' ability to borrow the amounts needed to get on the property ladder in many parts of the country.

We believe that meeting this new challenge requires the development of a truly flexible savings product that could facilitate both pension saving (with ability to benefit from tax relief and employer contributions) with the ability to also save to buy a house without incurring any penalty for withdrawing funds from the pension early.

Given the overall responsibility that this product would place on individuals we also believe that a robust advice and safeguarding framework would be required. However, we believe this could be developed to be consistent with and proportionate to wider safeguarding frameworks at older ages around Freedom and Choice.

3. To what extent are financial services providers currently meeting the changing needs across different age groups? How could innovation in product design help meet changing consumer needs of different age groups?

We believe there is a lack of flexible savings products. In particular, the Lifetime ISA was introduced in a way that did not allow "joined up" savings, and so has not been widely embraced by consumers.

For example, at present, in order for pension savers to take full advantage of favourable tax treatment and employer contributions it is necessary to have a traditional pension fund which is not accessible until age 55 (or later). At older ages, this works extremely flexibly, allowing pension savings to be legitimately reallocated toward otherwise competing savings needs (such as potentially significant lump sum payments to pay off mortgages).

For younger generations who want to allocate pension savings to the same competing needs e.g. house deposits (which are part of the same property transaction), pension savings cannot currently be used without attracting a penal tax charge of 55%.

To avoid this, if an individual determines (perhaps quite rationally) that purchasing a house is a higher priority in the short-term than saving for their retirement they will lose out on the tax advantages and employer contributions of a pension.

To address these issues, we believe younger generations need flexible savings products that can meet their competing savings needs in an efficient way (without locking savings to a specific purpose that may not be the most effective use of their savings at any given time).

4. Are there any barriers (including FCA regulatory barriers or barriers to competition) that are adversely affecting access to, and use of, financial products that would meet new and changing consumer needs? Are these affecting particular age groups? If so, in what way? How should we address these while ensuring consumers still receive an appropriate degree of protection?

Legislation, for example for auto-enrolment, favours saving for retirement over other forms of savings. Freedom and Choice has provided flexibility for those over age 55 who can divert their retirement savings to other purposes should they wish (many choose to pay off their mortgage with their pension fund, for example). Those under age 55 have no such flexibility (for example, to pay the deposit on a house).

Unfortunately, it appears difficult for firms to provide significantly more flexible savings products without new legislation.

5. Is there anything more that we could do to encourage and enable positive innovation in these sectors, or to enhance competition in the interests of consumers?

We would like to see a more flexible approach to the legislation and regulation of long-term financial products. At present there are a relatively few products that are widely accessible to encourage long-term saving - for example, a pension scheme, ISAs, or Lifetime ISAs.

However, the legislation enabling these products is very prescriptive and restrictive. This leads to very little differentiation or innovation in the market. A flexible approach that allows firms to design their own products satisfying general principles that Parliament feels are important (such as preventing frivolous use of savings that have received tax advantages) would allow much greater innovation.

In relation to our proposals above, we welcome the wider industry focus and attention that has begun to emerge and we await further developments in relation to potential new product designs.

6. Is there any market or firm behaviour that causes or may cause potential harm to consumers? For example, is industry failing to recognise varying needs of consumers from different age groups and as a consequence, of this:
   a: offering products which may be unsuitable to certain age groups
   b: excluding, discriminating against, or failing to advance equal opportunity between certain age groups for no legitimate and objectively justifiable commercial reason (or where the reason is potentially legitimate but the approach is not proportionate)
   c: otherwise treating certain age groups unfairly?

We think there is a broad failure to appreciate the extent to which savings decisions have become more complex for consumers as a result of competing savings needs. While there has been a lot of recent innovation around products for the decumulation phase, there has been very little innovation in the accumulation phase.

For example, in reaching the conclusions set out in the Discussion Paper, we note that many of the financial assumptions used at early ages (shown in Table 1 of Annex 1) are almost identical for each generation, which we do not believe is appropriate.

We believe these factors are key to understanding the changing savings dynamics. For example, the assumption that at each age all generations will have an identical progression of household disposable income and weekly expenditure is not realistic. Whilst it may be the case that it takes on average nine years longer for Millennials to purchase their first property compared with Baby Boomers, it is likely their expenditure in real terms is higher owing to renting over the period. At the margins of disposable income, these are significant factors.

Moreover, the assumptions appear to ignore the impact the accrual of pension wealth in defined benefit form has had on older generations, compared with younger generations who have typically accrued pension in defined contribution form (as described in our response to Q1 and Q2).

The Discussion Paper's overall conclusion that outcomes are very similar over time for each generation therefore relies heavily on implied parity of many early years' savings factors which we think warrant further attention. Overall, in our view, this masks the impact of competing savings needs making a significant contribution to younger generations getting on to the property ladder much later in life, and accruing pension wealth in a much less favourable, and riskier, form.

At present, those in the accumulation phase, primarily younger generations, are offered broadly the same savings products that have been available for decades, despite there having been significant change in that time. Perhaps primarily because of legislative inertia, we believe this means the financial industry is failing to react fully to changing consumer needs and circumstances.

7. Are there areas related to intergenerational issues which fall more appropriately to Government or another public body, but in which, in accordance with our objectives, we can play a role? If so, which ones and in what way?

Many of the problems faced require legislation to rectify, so the involvement of government is essential.

If legislation is passed allowing more flexibility in the design of long-term financial products, then the FCA will play a key role in regulating the firms offering such products, as well as ensuring consumers have the information they need in order to make well-informed decisions.

APPENDIX 2

About the Association of Consulting Actuaries (ACA)

Members of the ACA provide advice to thousands of pension schemes, including most of the country's largest schemes. Members of the Association are all qualified actuaries and all actuarial advice given is subject to the Actuaries' Code. Advice given to clients is independent and impartial. ACA members include the scheme actuaries to schemes covering the majority of members of private sector defined benefit pension schemes.

The ACA is the representative body for UK consulting actuaries, whilst the Institute and Faculty of Actuaries is the professional body.

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Produced by:
Association of Consulting Actuaries Limited
First Floor (129)
40 Gracechurch Street
London EC3V 0BT
020 3102 6761
acahelp@aca.org.uk
www.aca.org.uk
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