Financial Services and Later Life
A Scoping Project
for the Financial Services Consumer Panel

Jackie Wells & Mary Gostelow

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Financial Services and Later Life

A Scoping Project

A Research Report

Prepared for

The Financial Services Consumer Panel

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- Understanding the value to IFAs of the services received from financial services providers.

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1 Key Findings and Recommendations

The findings of this report suggest that the Financial Services Consumer Panel is right to include 'Financial Services in Later Life' among its key, pro-active areas of interest. Whilst much has been done and is being done to address consumer detriment for those in this lifestage, the market remains far from perfect. The Panel has the ability to apply an independent perspective to consumer detriment in later life and to influence key stakeholders operating in the market, including FSA and Government.

Consumers in later life suffer from a lack of information, guidance and advice across a wide range of financial markets. This can lead to inertia and lost opportunities to maximise income in retirement or for social engagement. Whilst the FSA's financial capability work, including the money guidance Pathfinder, is extending the information and guidance available to all adults, it is not yet clear that later life groups are being reached in significant numbers. Moreover, whilst clarity is emerging on the details of the FSA's Retail Distribution Review, it is likely to be many years yet before it becomes clear whether it has achieved any narrowing of the advice gap.

Limited access to affordable insurance products for those in later life is a source of discontent to many in later life. Whilst market initiatives are being sought to address these, changes in age discrimination legislation are likely to force through some further changes to the market. The eventual outcome for those in later life is uncertain however. Increased access may also come with increased costs and prices.

Products encountered by those in later life continue to grow in complexity. Whilst decisions around traditional annuities are far from simple, new products being developed to meet the needs of those in retirement add to the complexity of decision making. A lack of clarity over the risks associated with some decumulation products could place those at retirement at risk of making poor choices and, in time, lead to individual detriment as well as greater costs for the tax-payer.

Financial decisions in later life are already complex and can be made more so by individual circumstances; whether by ill-health, loss of physical or cognitive functions, a reduced social network or an inability to access new technologies. For an increasing number of people, the need for some form of social care, whether domiciliary or residential, brings with it a number of difficult financial decisions. In the near future, whether in this or a subsequent government, the landscape for funding social care is almost certain to change. This change, whatever its shape, is likely to lead to even more individuals in decisions about funding and in turn increase the need for clear information and guidance.

Increased financial complexity for the growing numbers of individuals who have entered the decumulation phase of financial life appears to be inevitable. Increased complexity brings with it the potential for increased consumer detriment. In such a world, the role of the Panel in monitoring, researching and intervening in the regulation of later life markets intensifies.

1.1 Project Objectives

The Financial Services Consumer Panel has identified later life and financial services as one of its most significant areas of interest. It commissioned this initial scoping paper to help identify whether there is cause and scope for the Panel to progress with further research or to consult with the FSA and/or Government on areas where detriment appears to exist. The objectives of the project were:

- To identify and define the key financial issues facing consumers in later life;
- To address these issues against the panel's prioritisation criteria and capability;
- To propose a high level strategic response through which the panel can act / intervene.

1.2 Finance and later life

Finance in later life is different in many respects to earlier financial decisions, and yet many of the mechanisms for delivering financial services to those in later life are not adapted to take account of the differences:

- Many decisions may be critical, stressful and irreversible and yet broadly the same standards of advice are applied to later life decisions as are applied to earlier life decisions.
- Products and the consequences of those products are, in many cases, different to those encountered in earlier life. Increasing numbers of consumers can expect to encounter products in later life for which they have no previous experience; in effect, starting with a blank sheet of paper in terms of their product knowledge.
- Decisions are made more complex by the interaction of individual needs, family needs, state benefits and taxation and by uncertainties over health and longevity and yet access to advice remains fragmented.
- A significant number of those in later life have limited access to information and advice which requires the use of new technologies. Meanwhile many industry developments (including the FSA's Financial Capability work) are understandably focused on how technology can be used to reach consumers more efficiently;
- Physical and cognitive Impairments in later life may, for some, limit their ability to make full use of the information and advice and the products that are available, and yet little is currently done to reflect this in the design of products and services or the delivery of information and guidance.

In this report, we consider a number of lifestage transitions, issues and risks specific to those in later life and the specific interactions which older consumers have with financial services markets. Section 3 of this report sets out in more detail how consumers in later life interact with financial services markets.

In each market we have examined: whether there is any empirical or anecdotal evidence for consumer detriment; the theoretical materiality of that detriment (if it happened, how significant would it be to the individual consumer or society as a whole); the causes of that detriment; and the probability of the detriment arising given market behaviour and existing or planned initiatives designed to remove, reduce or compensate. Our research and framework for considering consumer detriment are set out in section 4 of this report.

1.3 Assessing consumer detriment

The concept of consumer detriment has been developed extensively by the Office of Fair Trading and the FSA. In this paper, we develop a framework for considering consumer detriment which takes account of both the financial loss that an individual (or society) may suffer and the emotional or lifestyle loss that can occur.

We consider detriment to be attributable to actions (or inaction) associated with misinformation or lack of information on the part of the consumer. By way of examples, a consumer investing in the stock market in an informed way would not normally be considered to be suffering detriment if loss is incurred due to stock market fluctuations. However, a consumer investing in a product which exposed them to stock market risk in a way which had not been fully described or they were unable to understand could be considered to suffer detriment in the event of loss arising from movement in the stock market.

We also consider the non-financial consequences for consumers including social exclusion, confusion, stress and anxiety and associated health consequences, irrespective of whether a financial loss has occurred. By way of example, consumers who are unable to access car insurance may not suffer a financial loss as such but may well suffer from the stress of not being mobile and ultimately from some sense of social exclusion.

1.4 Analysis of markets

The findings from extensive desk research and a number of formal and informal discussions with stakeholders provided us with very considerable research material on the five markets summarised below. Details of the research examined in each market and the conclusions drawn on current or potential detriment are contained in sections 5 and 6 of this report.

Decumulation: The very importance of the decumulation market to those entering and in retirement combined with the complexity of the market make for one where consumer detriment is both feasible and significant. Many different interventions have been put in place to protect the consumer, and to a large extent markets are thought to operate efficiently. Overall, there is little evidence in any decumulation markets of poor value for money products, with competition working to limit charges. However, there remain widespread perceptions of poor value for money and some gaps in empirical evidence, in particular around alternatives to traditional annuities.

A number of initiatives in the market have sought to reduce the asymmetry of information, most recently in developments in the annuity market. However, consumer understanding remains low and the scope for misselling or misbuying high. FSA sales regulations limit the volume of misselling but where it does occur the consequences for the consumer can be severe, extremely stressful and in some cases difficult to remedy.

Consumers are protected against default by insurance companies and pension funds, although in the case of some products (income drawdown for example), the protection is limited to £50,000. Protection for those with annuities is close to 100%, for as long as insurance companies continue to be able to fund the FSCS. The level of protection afforded those with hybrid products is not clear and may require clarification. There are no indications of risk of their failure to do so but major improvements in mortality could present the industry with challenges. Those in DB schemes in default are protected (some up to a cap) as long as there are sufficient DB pension schemes to fund the PPF. There exist some concerns about the long-term sustainability of the PPF.

Protection Markets: There are pockets of perceived consumer detriment in protection markets. The main forms of detriment are lack of access to markets, opportunity costs and increasing social exclusion, in particular in relation to car and travel insurance. Overall, existing research suggests that the probability of financial loss is small but that emotional loss may be greater.

Age organisations claim that there is between £131 million to £1,180 million of consumer detriment for those over 65 years in motor and travel insurance[1]. The Department of Communities and Local government (DCLG) Impact Assessment on the Equalities Bill estimates that a 0-1% fall in travel and motor insurance premiums for the over 65's would represent savings of up to £16.5 million to older consumers, as well as helping them to maintain their independence and mobility for longer. The insurance industry however, claims that costs will rise if age is not permitted as a discriminator in motor and travel insurance.

Banking and credit: In recent years, the financial inclusion initiatives in banking and credit have reduced the risk of detriment among low income older people, while tighter regulation and increased compensation levels have reduced the potential for financial loss among older consumers. Nevertheless some older people still do not have a bank account (some by choice) and will suffer detriment arising from the 'poverty premium' incurred. The increasing use of technology in banking services, through 'chip and PIN' and internet banking will increasingly isolate those who lack confidence in accessing cash and making and receiving payments electronically or who do not have access to the internet. Although debt (either unsecured or relating to a mortgage) is not an issue for the majority of older people, where it does occur, its impact is likely to be more significant for those affected - those who owe money when they retire owe substantially larger amounts than their counterparts of ten years ago.

Saving & Investment: Recent turmoil in markets and economies has highlighted the lack of resilience that both consumers and financial institutions have to extremely difficult conditions. Whereas concerns in the past have been focused on equity-based products, much of the concern in the past year and many of the complaints against the industry have been focused on the banking and building society sector. The risk of major banking insolvency allied to a collapse in interest rates has made the previously 'safe' haven of cash much less comfortable. Many older consumers have experience finance loss, a much-reduced income and often considerable stress worrying about the security of their money. One bright light that emerges from the gloom is that consumers, particularly those relying on savings, are generally more aware of the risks they take and the remedial services that protect them.

Equity-based investment products continue to raise concerns, with the perennial uncertainty about the value for money of investment bonds and the costs and risks of structured products.

Information, guidance and advice: Whilst younger people are possibly better served than they have ever been, albeit that there is scope for information overload, older generations are often excluded from the growth in consumer-oriented information by:

- their inability or lack of desire to access new technology;
- for some, their lack of mobility or social isolation;
- for some, a lack of trust in financial institutions or enhanced sense of vulnerability;

[1] Experts' Working Group(2008) Age discrimination in financial services

- for others, their preference not to ask for help.

Whilst initiatives are underway to help fill the information and advice gaps for older people, it will be some time before we know whether they have been successful.

1.5 Where should the Panel focus?

Whilst there are a number of overarching issues facing those in later life – managing risk; managing lifestage transitions; managing ill-health, managing bereavement, all of which impact on an individual's financial position, it is also the case that some markets warrant more attention than others.

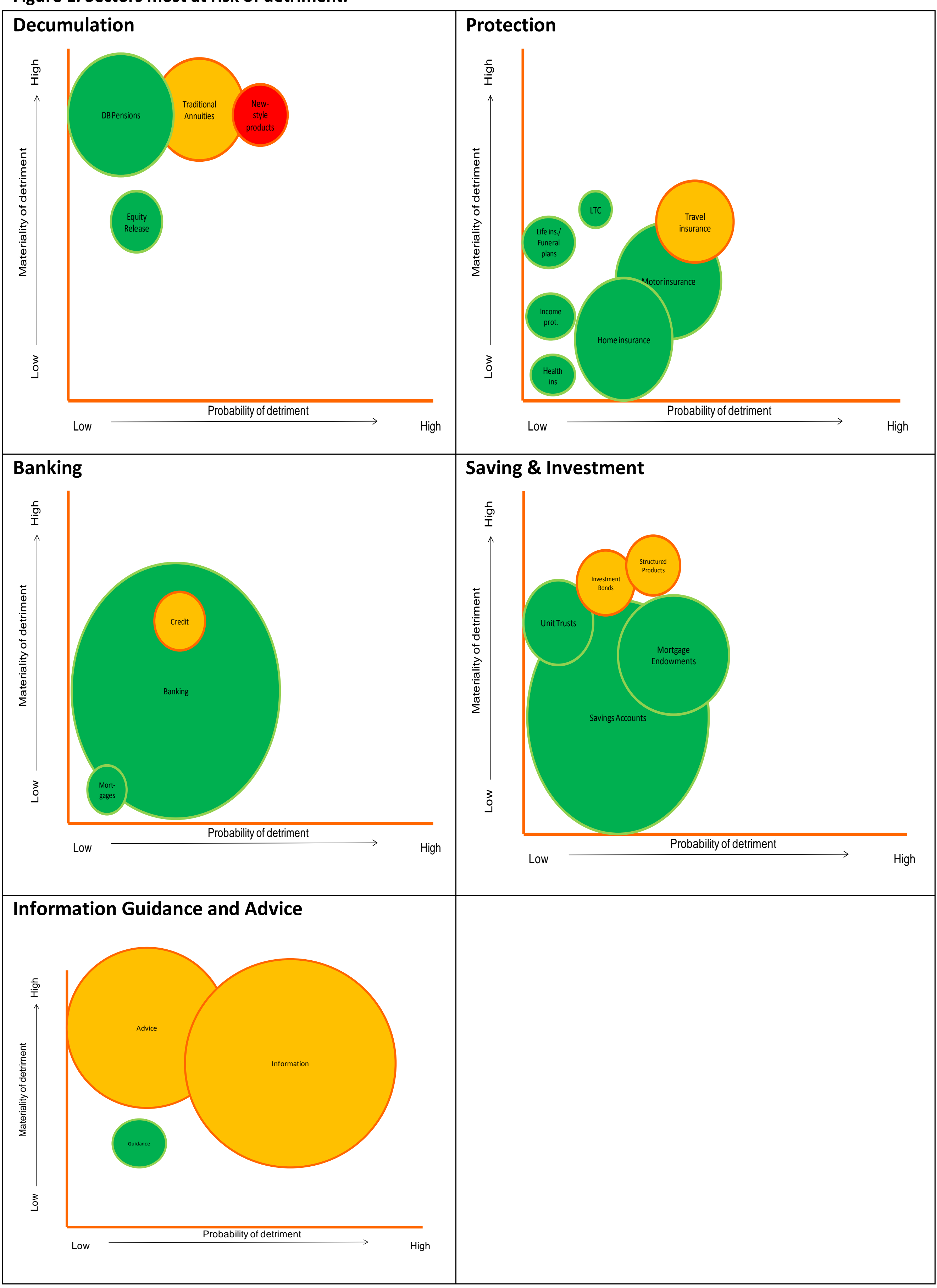
The charts below (Figure 1) are designed to be illustrative only and are not intended to measure with any precision the materiality or probability of consumer detriment in each market. Rather they seek to highlight those market sectors where detriment may be most significant or possible in today's environment (highlighted in red or yellow in the charts) and where the Panel may choose to focus its work. The size of the bubbles in the charts is an indication of the relative size of markets, although the nature of the shapes and words means that very small markets are difficult to show small enough in relation to very large markets, in other words, proportions are not exact.

In the decumulation market, two products stand out (in red or yellow). In the case of new-style annuities, there is little current evidence of (and no research) on detriment but concerns about consumers being missold such products and whether the products represent good value for money have been raised in recent times. Traditional annuities, whilst a much larger market is one where several areas of consumer detriment are being addressed but concerns about the lack of joint life annuities continues to be of concern. Given the importance of these products in helping consumers maintain their income in retirement, the detriment were it to arise could be very significant for both the individual and society.

In the traditional annuity market, whilst current initiatives can be seen to be reducing detriment, concerns still exist about levels of consumer understanding and the type of annuity being purchased. Broader concerns have been raised about the ability of advisers in this market to deal with the growing complexity of products on offer. Whilst DB pensions exhibit the potential for significant consumer detriment and concerns about the long-term sustainability of the PPF, at the present time, the probability of detriment appears to be quite low. The risk to the insurance sector from improving mortality continues to be highlighted by the FSA and the FSA industry should continue to be encouraged to monitor improvements brought about by biomedical advances.

By contrast, whilst there are a number of issues in the protection market that warrant further attention, the materiality of any detriment is likely to be less than in the decumulation market. The money at risk is less and any emotional detriment is likely to be proportionately less, although it is important not to play down the sense of social exclusion that can result from limited access to insurance products that facilitate mobility. Of all the markets, travel insurance would appear to be the one which warrants some attention from the panel.

Figure 1: Sectors most at risk of detriment.



In the banking sector, several initiatives are at work to reduce the detriment suffered by older people, notably the work of financial inclusion. However, the credit market remains one where potential detriment can be high for those few who find themselves with high levels of debt in later years of life. Inability to repay debt in later life can lead to very significant levels of stress with a knock-on effect on health and social inclusion.

In the savings and investment markets, the risks and costs of structured products and investment bonds continue to warrant attention, particularly in today's difficult market conditions. Asymmetry of information, high charges and complexity of risks can easily lead to the risk of misselling.

In theory, all those in later life will need information, guidance and/or advice at some point. However, for those who are financially capable or have a strong family or social network or have a relationship with a financial adviser the question of where and who to turn for information and/or advice may be less of an issue, though some may suffer detriment from poor advice. The potential for detriment is greater among those who do not know where to go for information and/or advice and lack the capability to fully understand the implications of the decisions that they might/might not take as a consequence. With the exception of those who fall within the remit of financial exclusion, it is difficult to identify exactly how many later life consumers could and do suffer detriment in this area.

The above analysis suggests that the Panel may choose to prioritise their work on later life in the following order:

1. Decumulation markets;
2. The provision of Information, Guidance and Advice
3. Savings & Investment markets;
4. Protection markets;
5. Banking markets.

1.6 A way forward for the Panel

In considering a strategy for the FSA we are guided by two factors: what role is appropriate given the Panel's terms of reference, and what the Panel is able to do with its limited resources. The panel is clearly not able to resolve any of the potential detriment through direct consumer action; it is neither resourced nor empowered to deal directly with consumers. We have also ruled out any major research initiatives (although there are some areas where the Panel may be able to devote some resource to further research). This leaves the Panel with options which range from maintaining a watching brief, through further research and into more active recommendations to regulators, in particular the FSA, industry, the Government and the third sector.

Our recommendations for the Panel are that it should consider adopting a strategy which includes the following elements:

1. The panel should consider making Later Life and Financial Services one of its key consumer-oriented areas of focus (as opposed to focusing on specific market sectors). A specific working group could be convened to review on an on-going basis the broad range of issues facing those in later life and to consider whether the risks of detriment in any of the markets in which older people participate have

been reduced or increased by interventions or market behaviour. The focus of the working group in the early years should be decumulation, savings and investment markets and Information, Guidance and Advice, but with a watching brief on developments arising from the Equalities Bill and developments in the credit market.

2. The Panel should consider adopting a cross-cutting role in helping to develop and shape a holistic view of the consumer in later life and encouraging further research. The Panel could leverage its independent position as a consumer group in financial services to engage with a wide range of interested parties including Government, regulator, industry, think-tanks and third sector. Particular areas of focus could include:

    a. The implications of the Green Paper on the funding of social care for older consumers and the industry;

    b. Developments occurring in response to the Equalities Bill, in particular reviewing the outcome of current research projects investigating the financial services sector;

    c. Review of forthcoming research on decumulation to develop a holistic view of the emerging issues (if any) and encourage further research in these by the contributors if appropriate.

3. In many areas of the market, research has either been completed recently or is underway. However, in areas where uncertainties remain, the Panel should consider whether it can be effective in commissioning further research. Areas which would appear to justify further research include:

    a. The pricing and risks of alternatives to traditional annuities. Do they represent good value for money? What opportunities and risks do they represent for consumers? Which types of consumer ought to consider such products?

    b. The delivery of financial information, guidance and advice to those in later life. What are the needs of those in later life? Are there ways in which advice can be delivered in a safer environment and with greater accessibility? How can the supply of advice be increased in an appropriate way?

    c. The Panel may wish to explore whether the Banking Code adequately deals with the risks associated with bank and building society accounts and whether those risks are adequately disclosed to and understood by consumers.

    Alternatively, if resources are limited, the Panel might consider encouraging other parties to commission research or forming a consortium to investigate these issues.

4. The Panel should construct a short list of issues to address back to the FSA. Our suggestions include:

    a. Decumulation. Are the risks to insurers and consumers of the new ‘third way’ decumulation products clearly understood in respect of solvency and suitability? Are the risks to annuity providers from medical advances fully understood and factored into pricing?

    b. Later Life advice. Are the standards of qualification and ethics for advisers to those in later life adequate and sufficiently well defined? Do existing examinations prepare advisers adequately for dealing with new-style decumulation products? Is there a need to set out a distinct set of ethics for the way in which advisers deal with more vulnerable consumers, including those in later life? Is there a need for guidance on the attitudinal / psychological profile of advisers suitable for dealing with those in later life (or by contrast, a profile of those unsuitable for

dealing with older customers)? Is there a need for any additional training to be provided to advisers dealing with older customers to make them aware of the significance of advice to those in later life? All of these questions could be directed to those dealing with professionalism within RDR.

c. Financial Capability - Can the FSA report on the progress of its financial capability strategy for those in later life? Has the Money Guidance / MoneyMadeClear Pathfinder been successful in reaching and providing guidance to those in later life and what needs have been identified? Is there a view emerging as to whether the Pathfinder is successful in helping people to reach successful outcomes?

In summary, we believe that there is a strong case for the Panel to further review and take up a number of issues relating to later life and financial services We suggest that the Panel considers implementing a four-part strategy based on review, engagement, research and constructive dialogue will help to identify and clarify any significant new detriment and help to drive forward solutions for addressing current concerns.

2 Project Approach and Objectives

2.1 Project Objectives

Whilst much of the work of the Financial Services Consumer Panel ('the Panel') is reactive to Financial Services Authority (FSA) thematic work and consultations, the Panel is also developing its own initiatives which it will review at regular intervals. These are areas where the panel considers there to be issues of significance for consumers and which meet the Panel's prioritisation criteria, which are:

- Is it a consumer issue?
- Is there actual or potential serious or widespread consumer detriment?
- Does the panel have the capacity / resource to get involved?
- Are other bodies involved on the same side?
- Will Panel intervention make a difference?

The Panel may use evidence from these initiatives to develop its own position over time, to commission further research, to respond to consultations covering the subject, to produce positioning papers or to adopt a more outward facing communication policy.

The panel has identified later life and financial services as one of the most significant areas of interest and commissioned this initial scoping paper to help identify whether there is cause and scope for the Panel to progress with further research or to advise the FSA and/or Government on areas where detriment appears to exist. The objectives of the project were:

- To identify and define the key financial issues facing consumers in later life;
- To address these issues against the panel's prioritisation criteria and capability;
- To propose a high level strategic response through which the panel can act / intervene.

2.2 Project Scope

It was agreed with the panel that the project should focus on the following:

- Issues relating to consumers (ie excluding financial services for businesses but including corporate pensions);
- Focus on those in the decumulation phase of life (following partial or full retirement) but with some reference to the immediate pre-retirement lifestage;
- All financial services products but with some emphasis on FSA regulated markets;
- Focus on markets where consumer detriment (specifically related to later life) is evident.

Because of the very broad nature of this report, it has not been possible to examine every issue facing those in later life in great depth. We have therefore chosen to focus on areas where there is existing evidence of detriment or concerns about future detriment. Moreover, we have chosen to focus on issues which are specific to those in later life, accepting as we do so that there are a number of issues faced by individuals of all ages that we have not been able to cover, for example, the issue of bank charges.

Later Life

The focus of this report is on individuals in later life. This lifestage lacks a universally accepted definition and many terms can be used to define this period of life for older people such as the grey population, later life and seniors. All these descriptors will in turn have different age definitions. Later life is defined by the Financial Services Consumer Panel (the Panel) as the period following the main accumulation of wealth and where an individual has substantively stopped working. During conversations with the Panel, this definition was refined to describe people who are in the immediate pre-retirement phase, as well as at retirement and in retirement. Using this definition, the later life phase might start as early as 50 years of age.

With a potential age range of 50 years to over 100 years of age, later life does not comprise a homogeneous group of older people. The definition itself does not distinguish between the 'young' old and the very old and therefore does not take into account the very differing experiences and needs of these extreme ages. Research for DWP in 2008[2] recognised three important sub-groups – those aged 50 to State Pension age (SPA); those between SPA and 75; and the over 75s. It was felt that these stages were distinguished from one another by factors such as employment, family life stage, relative incidence of health problems and disability and the extent of friendships and family support networks. Though the diversity of the later life group is recognised, the scoping nature of this project means that this report focuses generically on the key issues facing later life consumers. Where sufficient information is available and the differences are significant, commentary is made on discrete groups of older people.

Product Scope

As well as considering generic issues and risks facing those in later life, specific markets / products were researched. To facilitate the literature review, stakeholder discussions and feedback to the Panel it was discussed and agreed that the main financial areas would be grouped together. Five main groupings were compiled:

- Decumulation activities;
- Saving & Investing;
- Mainstream banking (for many the only financial activity);
- Protection;
- Information and Advice.

These groupings are described in more detail in later sections.

Detriment

The Panel's focus is on areas of consumer detriment. As part of this project we have sought to define how we look at consumer detriment in financial services markets, what detriment looks like, what its causes are and what remedies are already in place to address them or are in planning. We explore this issue in more detail in section 4 of this report.

[2] Sykes, W. and Hedges, A., with Groom, C. and Coleman, N. (2008), 'Opportunity Age Information Indicators Feasibility Study', Independent Social Research, for Department for Work and Pensions

2.3 Project Approach

The activities undertaken for this report were:

- A search and review of existing research reports and papers on the subject of key issues in financial services with a focus on how these impacted on older people;
- Limited number of interviews and discussions with key stakeholders such as the FSA, DWP, and commercial and third sector organisations;
- High level analysis of the desk research and stakeholder interviews to identify key areas where potential serious or widespread consumer detriment could or does exist, taking into account the impact of current and planned policy and regulatory initiatives;
- Gap analysis of market interventions;
- Identification of opportunities for the Panel to intervene as appropriate.

Throughout the project, workshops and meetings were held with the Panel to discuss and review findings and project progress.

Desk Research

The first stage of this project involved an extensive literature review of reports and papers relating to older people and financial services as well as more general papers relating to financial services (for example, financial inclusion) which were likely to contain relevant information relating to the key financial issues facing older consumers and their potential to experience consumer detriment.

The literature review was wide ranging and included documents from each of the following key sources:

- Government reports or consultations such as the OFT (Office of Fair Trading) surveys and reports on consumer detriment ;
- FSA thematic reviews, consultations and research papers such as Financial Capability, Finance in and at retirement;
- Academic research studies from King's College, London, Institute of Fiscal Studies;
- Data published by the Financial Ombudsman Service (FOS) and the Financial Services Compensation Scheme (FSCS);
- Third sector research such as Help the Aged, Age Concern;
- Consumer groups reports published by organisations such as Which? and Consumer Focus;
- National and trade press;
- Financial internet sites [need to take a look at debates on MoneySavingExpert.com etc;
- International research where applicable.

Documents are referenced in footnotes throughout the document. Where material has been helpful but not specifically referenced, it is mentioned in the bibliography in section 8.

The authors of this report also wish to draw attention to forthcoming research from the Government Equalities Office (due May 2009) which may further our understanding of consumer detriment in financial services among older people. This independent research was commissioned to:

- Examine the extent to which financial services are available to people across a range of ages;
- Explore how quoted prices for financial services differ for people of different ages, and whether this equates to claims data (that is, risk);
- Assess the role of age in determining product coverage and price;
- Identify the other evidence and commercial considerations financial services providers use to decide product coverage and price, including other possible risk indicators which are used in addition to age or could be used instead of age;
- Examine the advantages and disadvantages of limiting the use of age-based practices in line with the age sector organisations' preferences (as set out in the final report of the Experts' Working Group)[3].

Interviews

Interviews or less formal discussions were held with a small number of stakeholders as agreed with the Panel. These included two interviews each with the FSA and the ABI, interviews and discussions with the DWP Financial Inclusion team, DWP Pensions Communications and Policy team, Age Concern, Swiss Re, Saga, Which?, PPI, Financial Ombudsman Service, Aegon.

The purpose of the interviews and discussions with stakeholders was to:

- Obtain an overview of work they have conducted on the financial issues faced by consumers in later life;
- Obtain their views on how later life consumers are catered for in the current market and regulatory landscape;
- Challenge and validate at a high level the key findings from the desk research.

[3] Government Equalities Office (2009) Equality Bill Impact Assessment, TSO, London

3 Later Life and Financial Services

> ***"Many of the decisions that individuals make about retirement, health and housing in later life are complex and may be compromised by impairments in decision-making ability or other aspects of memory and executive function, including planning, organisation and mental flexibility."*** Banks, J (2006), Economic Capabilities, Choices and Outcomes at Older Ages, IFS, London

We make no apologies for repeating this quotation from James Banks, the co-author of many of the reports on the English Longitudinal Study of Ageing (ELSA); a quotation that was used recently by one of the authors of this report in a report for Age Concern England in 2008[4]. The excerpt summarises neatly why a continued focus on those in later life in relation to the financial decisions they make. Finance in later life is different to earlier financial decisions and yet many of the mechanisms for delivering financial services to those in later life are not adapted to take account of the differences:

- Many decisions may be critical and irreversible;
- Products and the consequences of those products are, in many cases, different to those encountered in earlier life;
- Decisions are made more complex by the interaction of individual needs, family needs, state benefits and taxation and by uncertainties over health and longevity;
- In the age of new technology, a significant number of those in later life have limited access to information and advice;
- Physical and cognitive Impairments may, for some, limit an individual's ability to make full use of the information and advice and the products that are available.

As our population ages and those in later life come to represent an even larger share of the population, it becomes even more important that we understand and respond to the financial needs and risks to which individuals and families are exposed and the way in which the market and state responds to those needs and risks.

Much has been written about the ageing of the UK population and its consequences for social policy, the economy and specific industries. Demographic trends mean that the number of those living for many years beyond retirement and this group represents a growing challenge and opportunity for the financial services industry. Whilst the opportunities for serving the affluent part of this market have been widely recognised and acted upon (e.g. through the growth in wealth management services), less research has been published which considers either the holistic needs of individuals or the needs across the segment as a whole. This is beginning to change as data becomes more readily available through the English Longitudinal Survey of Ageing (ELSA) and Government and the regulators begin to focus more on ageing and later life. Recent and current reports and studies which have focused on later life and financial services include:

[4] Age Concern England (2008), Beyond Financial Inclusion

- The English Longitudinal Study of Ageing (ELSA) has been running since 2002. As the name suggests, the study tracks individuals and households from the age of 50 onwards. The key subjects studied are health, quality of life and economic conditions. Several reports have been published which analyse the financial position of those in later life and how it changes post-retirement. We draw from a few of these reports in this research;
- Age Concern and Help the Aged have published a number of reports and books on the subject of older people and their finances including 'Beyond Financial Inclusion'[5] and 'Older Richer Fitter'[6]. They have also lobbied on subjects such as information and advice, equity release, bank accounts for all, debt and pensions;
- The Pension Policy Institute (PPI) is part-way through a three-part project on decumulation in later life. The first report has been published[7]and investigates the income needs of the retired. The second study is due to investigate the role of property and is due for release in July 2009 whilst the third report will look at the role of other savings and investments in retirement;
- In April 2009, AIFA and Prudential announced a major study into 'Income and Wealth in Retirement' with results due to be published in the summer of '09. The study is designed not only to paint the landscape of retirement and advice but also to consider whether consumer needs are met and to propose solutions to any gaps identified.;
- The FSA has published a number of specific papers on later life and financial services; the first a paper highlighting the issues arising from an ageing population[8]; a second [9] a follow-up paper setting out the FSA's proposed actions and a later paper reviewing the efficiency of the at retirement market[10]. More recently the FSA has conducted internal research into the financial capability needs of older people and has announced its intentions to focus on this sector in its forthcoming strategic developments. Further reference to the financial capability work is made in the section below on information, guidance and advice.

As mentioned above, later life brings with it many different and difficult financial issues. We explore below some of those issues in more detail.

3.1 Lifestage transitions

Later life is also a time when important life events and lifestage transitions occur, all of which have important ramifications for the household's financial position.

- Retirement: Whether or not individuals are in control of when they retire, that point in time can bring major financial decisions, of the kind not made before, a significant change in income levels

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[5] Age Concern England (2008), Beyond Financial Inclusion

[6] Metz D & Underwood M (2005), 'Older richer fitter. Identifying customer needs of Britain's ageing population, published by Age Concern

[7] PPI (2009), Retirement income and assets: do pensioners have sufficient income to meet their needs?

[8] FSA (2002), The impact of an ageing population on the FSA

[9] FSA (2002), Financing the future - Mind the gap, The implications of an ageing population – key findings and proposed actions

[10] FSA (2007), Finance in and at retirement – results of our review

as well as important changes in lifestyle and social networks. The FSA's 2007 report on retirement stressed the complexity of the decision making at this lifestage.

- Later life relationship breakdown: the over 60s represent one of the few age groups among which the rate of divorce is rising[11]. Divorce in later life, particularly following a long relationship can be extremely traumatic and complex. Very often one partner may find themselves with little experience of handling financial matters;
- Ill health (own or partners). Ill health can bring new financial challenges, in particular the funding of care needs. Finances may need to be reviewed and adapted and major decisions about restructuring made;
- Bereavement. The loss of a partner brings with it significant financial disruption. Whilst some individuals may find themselves with more assets in their own name than before, the vast majority will find themselves having to cope with a drop in income and having to manage the household finances on their own.

All of these transitions can result in very specific information and advice needs. We deal with these needs and the extent to which they are met in section 5.5 below.

3.2 Special Issues and Risks

Those in later life are also subject to a distinct set of risks, as highlighted on the Institute of Actuaries web-site[12]. They highlight the following risks for those post-retirement:

- Inflation risk: inflation is known to eat away at the value of those on fixed incomes. Whilst many retirement incomes are fully or partially linked to price inflation (or in rare cases, earnings), most of those who purchase an annuity purchase a fixed rate and most of those taking interest from their savings will find that the buying power of this part of their income falls over time. We discuss these risks under the decumulation and savings sections later in this report;
- Interest rate risk: recent market conditions have highlighted the extent to which many older people can have their incomes affected directly by changes in interest rates which affect their income from savings. Interest rates also affect the price of other financial products used in retirement, notably annuities;
- Stock market risk: Similarly, many older people with investments have seen their retirement funds and the income from them decline significantly in value in the past year or so;
- Business risk: all of those in later life are at risk to some degree or other from the potential collapse of a provider. In most situations, consumers will be protected by either the Financial Services Compensation Scheme (FSCS) or the Pension Protection Fund (PPF);

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[11] Saga (2007), http://www.saga.co.uk/magazine/relationships/couples/OverSixtiesDivorce.asp

[12] Institute of Actuaries, http://www.actuaries.org.uk/members/migs/topical_migs/ageing_population/post_retirement_risks

- Employment risk: whilst many of those in later life are not in employment, a growing number supplement their income through part- or full-time work and are at risk in an economic downturn. Age discrimination legislation affords some protection but enforced retirement can still be applied;
- Lack of appropriate information risk: this is a very real risk in markets where information asymmetry is widespread[13]. A lack of appropriate information places consumers of all ages at risk and can necessitate the use of financial advisers;
- Public policy risk: many older people are dependent on the state for their income and other support. This makes them particularly vulnerable to changes in policy;
- Longevity risk: nobody can predict with any accuracy how long they are going to live. Many people therefore run the risk that they will run out of money before they die. The traditional lifecycle approach to financial planning would advocate that individuals annuitise their assets in order to provide themselves with longevity insurance;
- Several lifestyle risks that can arise due to changes in personal circumstances, typically a decline in health or marital status that can result in a major change in financial well-being or in different needs such as housing, the need for care, or the needs of other family members.

3.3 Financial inclusion

The government's financial inclusion strategy has sought to ensure that "everyone has the opportunity to access the financial service products needed to participate fully in modern-day society"[14]. The emphasis of the work of financial inclusion is on those with low incomes and those suffering from multiple deprivation and, with one in five older people living in poverty, many older people are included in this group[15]. Several organisations, including Age Concern[16], National Consumer Council, Help the Aged[17] and Joseph Rowntree Foundation have pointed out the significant level of social and financial exclusion that prevails among older pensioners and/or those on low incomes, many of whom have for some time been dependent upon the cash economy. A recent report by the Personal Finance Research Centre (PfRC) for the European Commission also confirms that older people are among the most excluded from financial services[18]. Financial exclusion impacts upon the lives of older people in a number of key areas:

- A lack of financial products such a bank account, pension plans and insurance cover;
- Money management is more expensive. For example, savings made by paying through direct debit are unavailable;
- Limited opportunities to save money securely, leaving older people open to theft and unable to take advantage of savings rates;

[13] Sandler Review (2002), http://www.hm-treasury.gov.uk/d/ACF18E3.pdf
[14] HM Treasury (2007), Financial Inclusion: an action plan for 2008-11
[15] Help the Aged (2006), Financial exclusion among older people
[16] Age Concern England (2008), Being socially excluded and living alone in old age: findings from the English Longitudinal Study of Ageing (ELSA)
[17] Help the Aged (2006), Financial Exclusion among Older People
[18] European Commission (2008), Financial services provision and prevention of financial exclusion

- Opportunities to borrow from the high street are limited. Excluded older people are more likely to borrow from doorstep lenders or sub-prime lenders who may charge high levels of interest.

A number of initiatives have been developed to address these issues including the work on Basic Banking, the Post Office Card Account and the wider financial capability work.

3.4 Financial crime

Earlier in 2009, the OFT reported that each year UK consumers lose £3.5bn to scams. The average victim loses £850 and older people are the most targeted group.

In April 2009, the FSA announced plans to help protect older people from financial scams by working in partnership with Age Concern and Help the Aged. The project to help protect older people, is expected to be rolled out by autumn 2009, and builds on the efforts Age Concern and Help the Aged are already making to help them manage their money. FSA research[19] on people's awareness and attitudes to financial crime has found that older people are especially vulnerable to share fraudsters and other types of scams. Their research finds that 35% of people targeted by share fraudsters in the last year were over 65 years old. A brain scan study by Stanford researchers may help explain why older people may be vulnerable to scams. It found that older people are positively aroused at the prospect of making money, while emotions and brain activity that might make a person more circumspect and concerned about the risk of losing money, are dampened[20].

3.5 Financial abuse

Elder abuse in general has become a European-wide issue. AGE has published a report on the subject[21], whilst NIACE in the UK is undertaking a major research project into the abuse of older women[22] and Comic Relief has devoted considerable funds to researching and fighting elder abuse in the UK.

Estimates vary on how many older people experience financial abuse. The King's/NCSR researchers[23] say that the true proportion of UK people aged 66 and over who have experienced financial abuse during 2006/2007 lies somewhere between 0.32 and 1.35 per cent, in 2007, Action on Elder Abuse[24] estimate that 1% (86,500 individuals) experience financial abuse, while in 2008, Help the Aged estimate that between 0.5 and 2.5 per cent of all older people living at home admit to experiencing some form of financial abuse[25]. Whatever the actual number abused, the impacts on the older victim such as emotional distress, social isolation, depression and loss of self-esteem and self-confidence were typically experienced across a wide range of different cases[26]are often multiple.

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[19] The FSA programme of research on 'The scale and impact of financial crime' is still ongoing

[20] Older people react more calmly to the prospect of financial loss http://longevity.stanford.edu/about/pressreleases/olderadults Accessed 22 April 2009

[21] Age (The European Older People's Platform), Elder abuse - a SERIOUS concern for the EU

[22] NIACE (2009), http://www.niace.org.uk/news/niace-wins-bid-for-programme-against-elder-abuse

[23] O'Keeffe M., et al (2007) *UK Study of Abuse and Neglect of Older People: prevalence survey report,* London: National Centre for Social Research

[24] Action on Elder Abuse (2007) Briefing Paper: The UK Study of Abuse and Neglect of Older People 2007

[25] Help the Aged (2008) The Financial Abuse of Older People: a review from the literature

[26] Mowlam, A et al (2007) UK Study of Abuse and Neglect of Older People: Qualitative Findings

Regulation has been used to improve the protection of older people. Legislation such as The Mental Capacity Act 2005 (which came fully into force 1 October 2007), the Fraud Act 2006 (which came into force 1 January 2007) and the Safeguarding Vulnerable Groups Act 2006 aim to improve the protection of older people from financial and material abuse but are recognised as having limitations[27]. There are a number of barriers that prevent people reporting or taking action such as physical frailty and the fear of being seen to make a fuss.

No Secrets[28], the government policy to protect vulnerable adults such as older people from abuse, gives guidance to local agencies who have a responsibility to investigate and take action when a vulnerable adult is believed to be suffering abuse, including financial abuse. However, a survey by the commission for Social Care Inspection (CSCI) in 2007 inspecting the implementation of *No Secrets* recommendations found that a sixth of all 150 councils in England were 'failing to safeguard adults well' with *No Secrets* poorly implemented in some areas. CSCI reported that council systems are not as tight as they should be and therefore cannot be guaranteed to respond adequately to adult protection referrals[29].

3.6 Age Discrimination

The use of age as one element of pricing is widespread in financial services. In some cases this benefits older consumers and in others is perceived to be a cause of detriment.

In April 2009, the government published the Equality Bill. This is expected to receive Royal Assent in Spring 2010. The purpose of the bill is strengthen existing legislation and bring forward new measures to fight discrimination. This includes banning age discrimination outside the workplace. The Equality Bill will make it unlawful to discriminate against someone aged 18 or over when providing services or carrying out public functions. The ban on age discrimination is intended to catch only those actions or omissions that result in genuinely unfair discrimination because of age.

In its impact assessment, the government concluded that "age discrimination appears to be most widespread and of greatest concern are financial services and health and social care"[30]. Despite consultation and work with stakeholders prior to the Bill[31], it feels that their work is not sufficiently robust to steer detailed implementation. The government is therefore conducting further work with the result that measures that specifically concern the financial services sector will follow in secondary legislation. This is expected to be implemented by 2012. At this stage of the Bill's progress it has been established that age exemptions in financial services are permissible and that appropriate age based treatment may include:

"... age differences in the calculation of annuities and insurance programmes which are reasonable and based on adequate evidence of the underlying difference in risk"[32].

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[27] Help the Aged (2008) The Financial Abuse of Older People, a review from the literature

[28] Department of Health and Home Office (2000) No secrets: guidance on developing and implementing multi-agency policies and procedures to protect vulnerable adults from abuse

[29] Help the Aged (2008) The Financial Abuse of Older People, a review from the literature

[30] Government Equalities Office (2009), Equality Bill – Impact Assessment

[31] Experts' Working Group(2008), Age discrimination in financial services

[32] Equality Bill volume I 2009

Currently in the UK, age is used by insurers as an indicator of the level of risk posed by an individual. Risk may be considered either by individual age as in life assurance or annuities where age is the major determinant of life expectancy, or by age bands as in travel insurance where age is commonly used as a proxy for health and mobility. The industry argues that this simplifies the underwriting and sales processes so that consumers benefit from a more competitively priced product. The existing approach has seen the emergence of firms who target specific groups of customers, by for example, age, income and/or lifestyle. Later life consumers are catered for by firms such as Saga, inTune (Help the Aged), Age Concern, RIAS and Castle Cover.

More generally however, age organisations such as Help the Aged and Age Concern have found evidence of direct and indirect age discrimination in their research[33]. In recent years, they have argued for legislation to ban age discrimination with specific reference to evidence from motor and travel insurances, where older people (aged 70 and more) experience difficulty in obtaining cover, either due to high premiums or the application of upper age limits. Throughout their arguments they have accepted that it is justifiable for insurance companies to use age where it is relevant to the calculation of risk, but not as the sole or primary proxy for risk. Not surprisingly, the industry through the ABI (Association of British Insurers) has argued that this is not the case and that the issue arises because some consumers do not know how to find insurance. Their answer is ""We should instead concentrate our efforts on helping older customers access the insurance that is available to them if they know where to look."[34].

However, not all age discrimination is negative. Within the financial services market, positive discrimination can be found such as:

- Savings accounts for the over 50s offering higher levels of deposits and paying monthly interest, sometimes higher interest, to make them more attractive to retired savers who are seeking income. It is not yet clear if these account will be exempt from the Equalities Bill;
- From 6 October 2009 the annual investment for people over 50 in an ISA will rise to £10,200, of which £5,100 can be saved in cash. Until 6 April 2010, the annual investment remains the same for other savers, tat is, £7,200 of which up to £3,600 can be saved in cash with one provider.

3.7 Market related issues

The bulk of the remainder of this report focuses on the interaction between those in later life and specific financial services markets. In addressing those markets we have grouped together financial activities. The five main groupings which are described in more detail below are:

- Decumulation;
- Savings & Investment;
- Mainstream banking activities;
- Protection;
- Information, Guidance & Advice.

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[33] Age Concern and Help the Aged (2007), Insurance and Age: exploring behaviour, attitudes and discrimination
[34] ABI (2009) Age and Insurance: Helping older customers find the cover they need

There exists considerable overlap between these five groupings, particularly in the area of decumulation. We have chosen, for example, to classify taking an income from savings and investment under that heading rather than as decumulation vehicles in their own right (since the accumulation and decumulation product is one and the same thing). Similarly, we deal with consumer credit under mainstream banking rather than decumulation, where it might also sit. We have chosen to write about information, guidance and advice as a separate topic but recognise and refer to issues that relate specifically to other products and services.

3.7.1 Decumulation

Many of those in later life will find themselves in the situation where they start to draw upon the rights and resources they have built up during a working life. The most common form of decumulation is drawing a state or private pension. However, some also start to turn their property assets into an income or lump sum (equity release). Others draw an income or capital from their savings and investments (see section on savings and investments below).

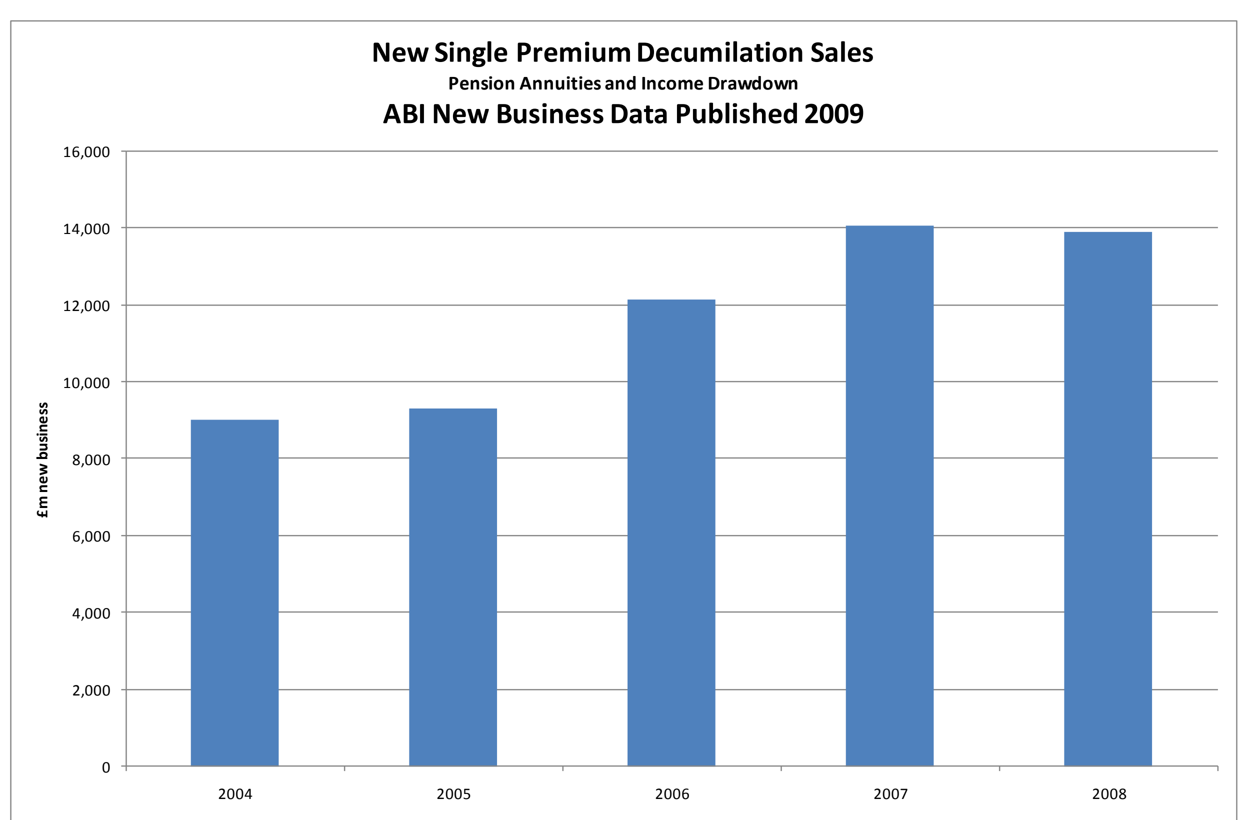
The decumulation market is a growing one, evidenced by the growing number of companies focusing on this stage of financial life and the emergence of new products. The market has also shifted from one where most of those drawing a private pension did so from a defined benefit (DB) pension scheme to one where a growing number have to choose whether to annuitise their retirement income or draw income from an alternative product. Decumulation decisions have become more complex for many people with an occupational defined contribution pension or a personal pension. The market is growing in size and complexity, increasing the need for financial capability on the part of individuals reaching retirement and the need for information, guidance and advice. The principle products available in this market are summarised below.

At retirement, some individuals will have the choice of a wide range of products, some of which will secure them an income for life, some of which will provide an uncertain level of income but provide continued exposure to stock markets and some which sit in the middle ground.

The Financial Services Baseline Survey suggests that approximately 4.7 million households are in receipt of either an annuity or income from a personal pension (1.4 million) or an occupational pension (3.6 million). 0.4 million households receive both.

Data from the Association of British Insurers) show that the value of decumulation product sales by value has been rising in recent years (see Figure 2 below). Whilst the number of contracts is not published by the ABI, the number of contracts is likely to have increased at a faster rate with values being impacted by volatile stock markets. The ABI has also reported that, in 2006, 93% of sales of pension annuity products continue to be traditional annuities whilst 5% are based on enhanced or impaired life rates and 2% are unit-linked or with profits. Annuity sales continue to represent the majority of the decumulation market. However sales of new-style ‘third way’ products are said to have increased significantly in 2008 (albeit from a low base) but may decline in 2009 with some withdrawals from the market.

Figure 2: ABI New Business data 2004 – 2008, New Single Premium Decumulation sales.



Traditional Annuities

These provide an income for the remainder of the individual's lifetime and, if selected, also a reduced income for their partner's lifetime. Key decisions that have to be made at annuitisation include:

- Whether to take a tax- free lump sum (and if one is taken, what to do with it);
- Whether to buy a fixed income for life, an increasing income for life or an index linked;
- Whether to choose a single or joint life contract;
- Whether to opt for a guaranteed period of income (income is paid for this period regardless of whether the individual survives).

Alternatives to traditional annuities

A wide range of products now exists which add to the complexity of the pension income decision. They include:

- With-profit annuities which provide an income for life to the consumer whilst maintaining a link to investment markets. Such annuities expose the consumer to investment risk and the potential for a lower income in the future if investment markets move against them, although most life companies set a minimum level of income below which the income cannot fall, even if there are no bonuses added. Market-value adjusters can be applied if the consumer later wishes to transfer to a guaranteed annuity. The fund remaining each year after income is taken is subject to charges in the with profits fund.

- Unit-linked annuities operate in a similar way to with profits but generally do not have a minimum level of income below which payments will not fall. Future income is determined entirely by the investment performance of the underlying fund and can rise and fall. The fund will be subject to normal unit-linked fund charges.
- A number of hybrid products that combine a lifetime income with some potential for investment / income growth(sometimes called 'third way annuities' or 'variable annuities', although the meaning of the latter expression appears to be inconsistent across the market). This part of the market remains small in the UK but grew fast in 2008 (up 53% in value in 2008)[35]. Several companies have entered the market in recent years, including a number of US companies who have developed similar products in the US. However, 2009 appears to have seen something of a reversal with the Hartford reported as pulling out of the variable annuity market in May 2009 and Standard Life delaying the launch of its product. Companies are reported as losing money on these products as the cost of guarantees rises[36]. These products sometimes involve the purchase of a temporary or term annuities that pay an income for only a fixed term (say 5 or 10 years), leaving the individual to generate an income for the remainder of their retirement from the remainder of their fund which is invested. Other products involve a combination of traditional annuities and investment growth. Some products are categorised as annuity products whilst others are categorised as income drawdown with guarantees. All of these products require the customer to annuitise at age 75 or to purchase an Alternatively Secured Pension (ASP – see detail below)). This annuity may or may not come with a guarantee and with some products could be less than the income taken before that age.
- Income Drawdown provides those with significant sums at retirement with the opportunity to remain invested (wholly or partially) in equities. The level of income that can be taken from the invested fund is determined a) by the size of the fund and b) by rules set out by HM Revenue and Customs. The rules are designed to prevent individuals eroding their pension fund excessively and to provide some protection over future income. Individuals who invest in equities before a period of market decline can see the value of their fund fall in value and their income fall as a result. Charges on income drawdown may include administration fees as well as investment management fees (part of which may be paid to the financial adviser). At age 75 an annuity or ASP must be purchased using the remaining fund.
- Alternative Secured Pension (ASP) is, as the name suggests, an alternative to the purchase of an annuity at age 75. It is available only to individuals who can demonstrate a principled religious objection to the pooling of insurance and mortality risk and has therefore a very narrowly defined market. In essence, an ASP is a continuation of Income Drawdown beyond age 75 for those who qualify, but with different rules setting the minimum and maximum amount of income that can be received and different rules applied to any residual fund on the death of the pension holder[37].

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[35] Money Management, April 2009

[36] Money Marketing, May 2009, http://www.moneymarketing.co.uk/cgi-bin/item.cgi?id=185654&d=340&h=341&f=342&nl=MM_BN&dep=webops&dte=010509

[37] HMRC rules on ASP, http://www.hmrc.gov.uk/pbr2006/pbrn13.htm

DB Pensions in Payment

A significant proportion of today's retirees receive their private pension from a DB scheme, based upon the number of years in that scheme and their income when they left the scheme (uplifted to take account of inflation). Government data estimates that around 60% of pensioner households receive some form of occupational pension income (much of which will be defined benefit for the today's cohort) with average weekly amounts being £156 for those in receipt[38]. Barring collapse of the employer or fraud, incomes from this source are protected.

Equity Release

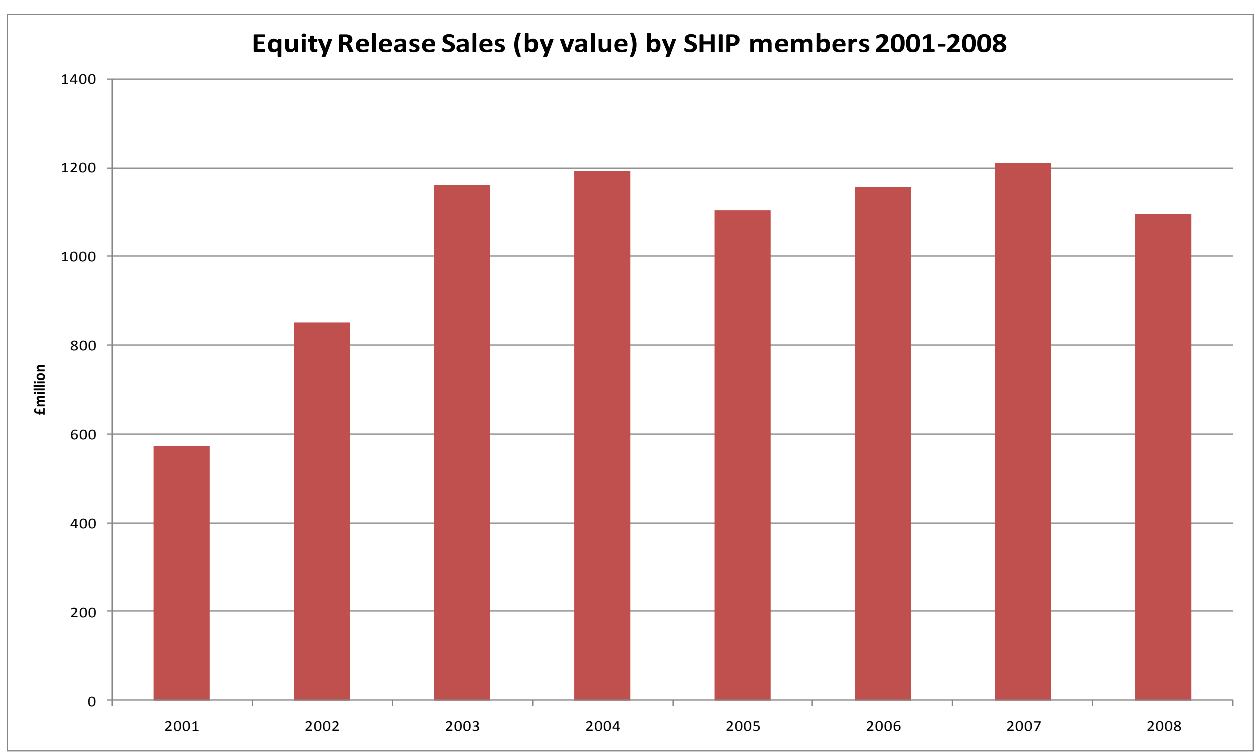
Finally, a small proportion of the population may choose to formally extract value from their property (usually their home) through a variety of equity release mechanisms. A much larger proportion may choose to release equity by selling and down-sizing their property. Equity release comes in two main forms with one further design now subject to regulation. These are:

- Lifetime mortgages. These products resemble a traditional mortgage product but the customer pays nothing back until they die (or their surviving partner dies). Interest is typically rolled up and added to the sum borrowed, although the total amount owed will depend upon how long the person lives. Many (but not all) products of this kind will include a negative equity guarantee which means that the amount owed on death can never exceed the value of the property. There are variations on lifetime mortgages including Home Income Plans, where the lump sum is used to provide an annuity income from which interest is deducted.
- Home Reversion plans. Rather than mortgages the home, part or all of your property is sold to a reversion company in return for a monthly income and/or a lump sum. Ownership passes over and the individual or couple become tenants with the right to continue living in their home rent-free (or sometimes for a nominal rent) for the rest of their lives. The reversion company receives the proportion of the sale proceeds (typically on death) that it purchased. Owners selling their whole property to a reversion company are likely to receive between 30% and 60% of its value as a lump sum (or an annuitised equivalent) due to the length of time it may take before the company gets its money back.
- Sale and rent back. Not technically included as equity release, this vehicle involves the sale of one's home to an organisation (sometimes a charitable institution), usually at a discount to its market value, and then renting it back, paying a normal rent for the property.

Sales data from the Safe Home Income Plans (SHIP) shows that the market for equity release fell slightly in 2008, a reaction in part perhaps to the fall in house prices (see Figure 3 below). CML data suggests that in excess of 125,000 lifetime mortgage contracts are in force. OFT data (based on Mintel and SHIP data) suggests that around 30,000 contracts are being sold a year. OFT estimates that 50,000 sale and rent back contracts have been undertaken up to 2008.

Figure 3: SHIP Sales Data 2001-2008, Equity Release Sales by Value

[38] DWP (2008), The Pensioners Income Series 2006-07



Section 5.1 considers in more detail the issues facing consumers in the decumulation markets.

3.7.2 Protection

The protection market splits broadly into two groups:

- Long-term insurances such as life cover (often sold as funeral plans to those in later life), long-term care (LTC) insurance, longevity insurance and income protection and
- General insurance (personal lines) particularly travel, motor, home and pet insurance.

Of the two, the general insurance market affects a higher proportion of the later life population as most households will require some form of cover. However, the life sector can provide for cover at critical lifestages such as illness and bereavement.

Long term insurances

Long term insurances offer later life individuals peace of mind as they provide a way of leaving a lump sum to families, ensuring that funeral costs are covered, paying for care if health deteriorates or potentially providing an income if you live too long. However, there are a number of factors which account for the small size of the market relative to other financial services markets, the prime one being the lack of product provision in both the LTC and the longevity insurance markets. There are no providers in the market for pre-insured long-term care insurance and only AXA and Partnership Insurance offer immediate care annuities. The fledgling longevity insurance market lost it sole provider, LifeTrust, earlier in the year in response to the financial markets turmoil and the high cost of delivering guarantees. The only long term insurance market displaying growth at the present time is the funeral plans market. The Funeral Planning Authority reported almost 11% growth in new sales to 74,683 plans in 2008 while undrawn plans increased by almost 6% in 2008 to 514,748, while insured funeral plans grew by 20% to 30% over the past year.

General insurances

Product holdings within the general insurance market vary extensively. The largest market is motor insurance as 3rd party cover is compulsory. Department of Transport data indicates that there over 15 million driving license holders aged 50 and over. However it is recognised that not all of these will still continue to wish to driver either due to declining heath or lack of confidence. Using data from Age Concern and Help the Aged's report 'Insurance and Age: exploring behaviour, attitudes and discrimination', it is estimated that the potential later life market in travel insurance is 6.5 million people aged 65 and over who travel at least once a year. Analysis of the FSA's baseline survey of financial capability suggests that among the over 50s ownership of home insurance is higher than most other groups with 78% having contents cover and 68% buildings insurance.

Section 0 of this report considers whether detriment arises in these markets.

3.7.3 Mainstream banking (for many the only financial activity)

Within the past decade, there has been a major change in how people conduct money transactions. Though the UK is still a cash-based society for smaller daily transactions such buying a newspaper or milk, technology has changed the way people carry out many of their daily money transactions. The increased use of technology, as exemplified by chip and PIN debit and/or credit cards, the increasing availability and convenience of ATMS compared to bank branches, the move to direct payment of benefits into bank account and the growth of online retail and internet banking, have changed the way people deal with money. The 'cashless society' is a growing one with plastic cards accounting for 66% of all UK retail spending in 2008[39].

Compared to the cash based society that they grew up with, the impact of these technological changes will have increased the complexity of money transactions for some older later life consumers. This section looks at three main areas within this market; current accounts, consumer credit and mortgages. Though a credit product, mortgages are considered separately because of the long term nature of the loan (typically 25 years).

Current accounts

Mainstream banking is the main, if not only, financial activity among many consumers. The majority of the later life population hold at least one bank account/Post Office Card Account, though it is estimated that 600,000 people aged 65 and over are without access to banking facilities[40]. Some of those without an account may have chosen to remain so. The main types of bank account held include:

- Post Office Card Accounts (POCA): Though these are not strictly a bank account, for an estimated 2 million pensioners they offer an electronic means of accessing their benefits. They work like an electronic benefits book and though money can be withdrawn, there are no transactional or direct debit facilities.

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[39] Payments industry publishes 2008 spending data, APACS press release www.apacs.org.uk/09_04_28.htm accessed 25 May 2009

[40] Financial Inclusion Taskforce (2008), Third annual report on progress towards the shared goal for banking

- Basic Bank Accounts: These are positioned as a potential way into banking for vulnerable groups. The allow consumers to use essential banking features such as paying in cheques for free, getting money at cash machines and paying bills by direct debit or standing order.
- Current accounts: These have more features than basic bank accounts which include a cheque book and overdraft facilities often with telephone and internet banking. Some current accounts pay interest on money left in the account but this is usually low. Those of these accounts offer free banking if the account is either in credit, retains a minimum monthly balance or a minimum monthly deposit is made. Many banks now offer accounts with extras such as travel insurance or roadside assistance for a monthly fee.

Credit

Credit comprises a wide and diverse range of products and services including: personal loans; credit and store cards; credit linked to the purchase of goods or services (store credit, hire purchase, conditional sale); cheque cashing and pawn-broking. If people have a poor credit record sub-prime lenders may provide a source of more expensive credit. These consist of authorised lenders such as home credit firms or loan sharks who are unlicensed lenders.

- Personal loans: These may be secured, using your home as security or unsecured.
- Credit and store cards: These have a spending limit based on creditworthiness and higher rates of interest compared to a bank personal loan.
- Credit linked to the purchase of goods or services: Payment of an initial deposit followed by monthly payments over an agreed period.
- Cheque cashing: Charges incurred are a handling fee plus a percentage of the value of the cheque. An estimated 6 million people use this service but they are less likely to be older people.
- Pawn broking: Enables people to borrow small sums of money over a short period of time by turning goods into cash with interest paid.

It is estimated that almost 5 million people aged over 50 have either some credit card or some other kind of outstanding debt.

Mortgages

Mortgages are still a small market in relation to people in later life, as most will have paid their mortgage by the time they reach 65 years. It is estimated that one in three UK pensions have mortgage debt after giving up work[41] and that about one in 20 older people have mortgages into their 80s.

In section 5.3 the potential detriment issues in mainstream banking that face people in later life are considered.

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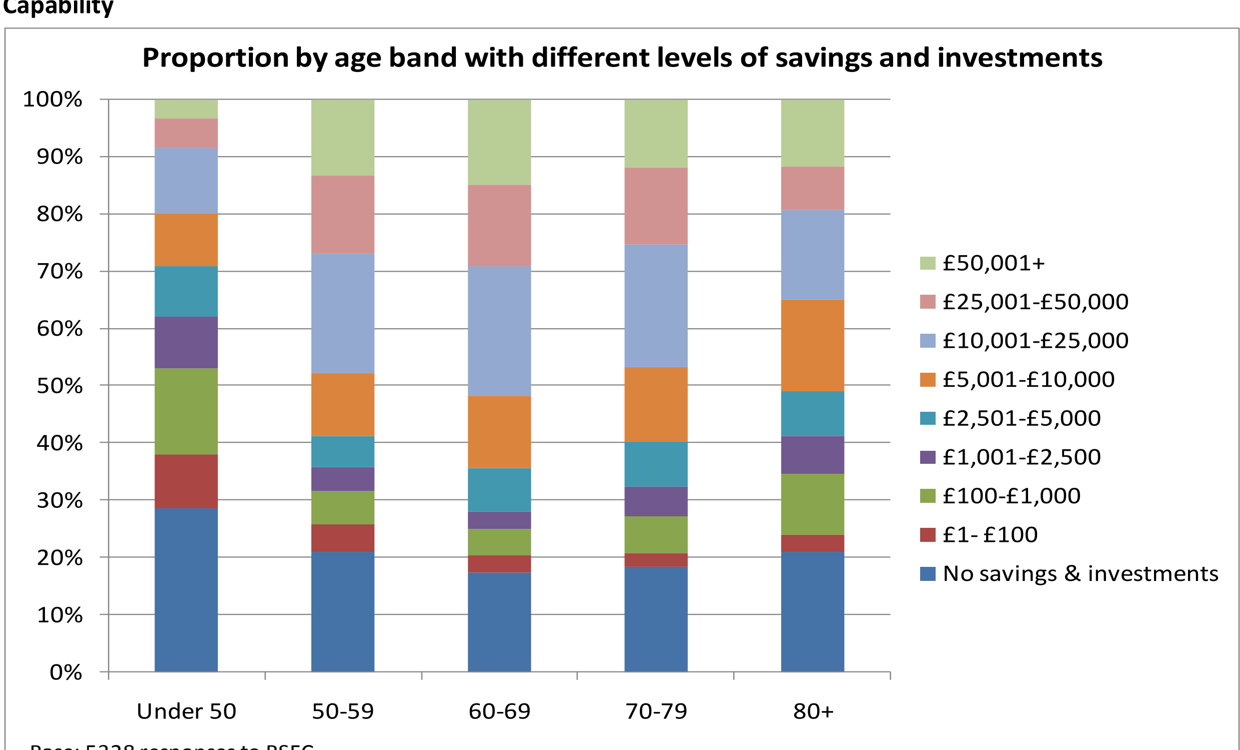
[41] Third of pensioners 'left facing mortgage debt' www.thinkmoney.com/mortgage/news/pensioners-mortgage-debt-advice-0-1461.htm accessed 19 May 2009

3.7.4 Saving & Investing

Data from the Financial Services Baseline Survey of Financial Capability produced for the Age Concern report 'Beyond Financial Inclusion' shows that more than 80% of those aged 50 and over has some savings or investments and that around 25% have more than £25,000. The same report indicated that around 60% of those aged over 50 save something in a year and that average savings amount to £2,000pa (likely to be highest among the pre-retired and considerably lower among the oldest retired groups). The retired not only save for themselves but also for their children and grandchildren (often for the latter through a child trust fund). The most popular form of saving remains the bank or building society account; but national savings are also popular among older consumers.

Figure 4: Proportion with Savings and Investments (by age and value). Source: FSA Baseline Survey of Financial Capability



The product holdings of older people are diverse. They are over-represented in terms of their share of the savings and investment markets across a number of products including Investment Bonds, Investment ISAs, Unit Trusts, Cash ISAs, direct share holdings, Premium Bonds and other National Savings products. Whilst some of these products are relatively straightforward and consumers may feel that they understand the risks (or at least did until the recent turmoil in the banking sector), many packaged investment products are more complex and expose consumers to a wide range of different risks and have different cost structures.

We consider how well the savings and investment markets work for consumers in section 5.4 of this report.

3.7.5 Information and Advice

The need for financial information, guidance and advice does not go away once an individual has retired. Indeed, given the major events that can occur later in life that present new issues for individuals and couples, the need can be greater than ever. However, the type of help required will vary according to the financial resources of the household. Those with few resources and with a great dependency on state

benefits may find themselves in need of help in claiming their full entitlement to benefits, entitlements which may change if ill-health is experienced and on bereavement. Those with very considerable financial resources may continue to need regular advice from a financial adviser as well as occasional legal advice in order to optimise the management of their finances for themselves and their families. Those who find themselves between these two extremes may find themselves in need of more occasional advice on financial planning, making a will, claiming benefits and coping with major life events. Many, regardless of their income, will find themselves in need of information and advice on funding social care in later life (for themselves or another family member), a subject which involves complex interaction between personal assets and state benefits. In section 5.5 of this report we consider whether the information, guidance and advice needs of those in later life are provided for by the market, government and third sector and whether gaps in coverage exist.

4 Consumer Detriment

det·ri·ment *–noun* loss, damage, disadvantage, or injury.

This research is focused on the current and potential detriment that faces those managing their finances in later life. Consumer detriment is itself the subject of several investigations and research projects. The Office of Fair Trading, the FSA and the EU have all produced reports on the subject, some defining the concept, others measuring the effect.

Previous studies have concluded that that there is no universally accepted definition of the term "consumer detriment"[42]. Nevertheless, the authors' review of the literature, as summarised below, has identified common themes which have informed our development of a framework for considering consumer detriment in financial services.

4.1 OFT and the concept of consumer detriment

Today's concept of consumer detriment has its origins in the OFT's series of surveys of consumer dissatisfaction which started in 1984. This led to the OFT commissioning research in 1996 to answer the question 'How should consumer detriment be defined?'. The report concluded that detriment can be defined only in relation to avoidability, that is, "the loss to consumers from making misinformed or uniformed choices" [43]. Consumers may or may not be aware of this loss. Using this definition, loss which arises from an informed decision would not constitute consumer detriment, for example consumers who invest in equities in an informed way and suffer loss due to stock market falls would not be considered to be subject to consumer detriment.

The concept was further developed and refined in 1999 in a paper by Richard Vaughan of University College, London on 'Distributional Issues in Welfare Assessment and Consumer Affairs Policy', and was attached as an appendix to the OFT's report on 'Vulnerable Consumers and Financial Services'. This applied a simple model to demonstrate that the loss of £10 is much more significant to someone with an income of £100 per week than to someone with an income of £1000 per week. This confirmed that the level of consumer detriment may be very different across different groups of individuals. With specific reference to insurance, this report (p.27) also noted that consumers can suffer detriment when:

- "Differences occur in premiums not related to expected cost of the insured event; or
- Premiums do not adequately reflect differences in risk (Squires 1998)"

These forms of detriment are clearly important when considering how age is used as a discriminator in the insurance market, a subject to which we return in section 0.

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[42] Europe Economics (2007), An analysis of the issue of consumer detriment and the most appropriate methodologies to estimate it. Final Report for DG SANCO, Europe Economics, London

[43] OFT (1997), Consumer Detriment under Conditions of Imperfect Information", prepared for the OFT by London Economics, Research Paper 11, London, OFT, p. 60

Subsequent OFT research (2006 and 2008) has sought to measure the financial impact and to understand better the financial and non-financial impacts of consumer detriment and to develop a methodology which could be used to identify the causes and effects of consumer detriment and who was susceptible. The most recent OFT definition of consumer detriment defines it as: "a measure of the financial losses suffered by consumers as a result of unsatisfactory purchases of goods and services"[44].

To specifically explore the non-financial impacts of consumer detriment, Dr Peter Lunt[45] conducted a literature review for the OFT about the problematic psychological effects of consumption when something goes wrong. This review concluded that psychological detriment has many potential dimensions and is exceedingly complex and variable between individuals because it can occur during decision-making, during interactions with sellers and/or after purchase (e.g. regret). Also, it can be long or short term in nature and can be related to specific shopping instances or to a person's worldview and basic values. According to this report, those traditionally perceived as vulnerable consumers, such as the elderly have characteristics that make them susceptible to incurring emotional costs. These characteristics include short time horizons, lack of cynicism, pessimism, lack of confidence, higher preferences for stability, and avoidant approaches to stress and challenge. However, susceptibility to psychological detriment can have a great many other causes not confined to the characteristics traditionally associated with vulnerable consumers, including mood, temperament, loss aversion, susceptibility to advertising and social isolation.

4.2 FSA and the concept of consumer detriment

One of the aims of the FSA is to ensure that "consumers are better able to make informed choices and achieve fair deals". From this perspective, consumer detriment arises when consumers are:

- "Not buying the best value products on offer, that is, the products that give them the desired level of quality at the best price and/or
- Not buying product suitable to their needs. This may include consumers' not saving at all, because they find financial decisions too difficult"[46].

Independent research for the FSA explores the concept of consumer loss in the context of poor financial advice[47] and attempts to identify drivers of consumer loss from poor financial advice by personal investment firms. This research further developed Europe Economics' concept of consumer loss as defined in their 2007 report for DG SANCO "An analysis of the issue of consumer detriment and the most appropriate methodologies to estimate it" as described in the section below. Consumer detriment is identified as arising from:

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[44] OFT (2008), Consumer detriment Assessing the frequency and impact of consumer problems with goods and services, OFT, London

[45] Lunt, Dr. Peter et al (2006), The psychology of consumer detriment, prepared for the Office of Fair Trading, OFT, London

[46] FSA Losing interest: How much can consumers save by shopping around for financial products? Occasional Paper 19, FSA, London

[47]FSA (2009), Firm-level Predictors of Consumer Loss Through Poor Financial Advice Independent research for the FSA by Europe Economics, FSA, London

- Structural consumer detriment — consumer welfare loss compared with a well functioning market outcome and
- Ex post consumer detriment — actual consumer losses experienced compared with reasonable expectations.

In the context of this study, personal loss is determined to represent a useful measure of consumer detriment.

4.3 EU and the concept of consumer detriment

Europe Economics[48] was commissioned by DG SANCO to analyse the issue of consumer detriment and the most appropriate methodologies to estimate it. Their review examined insights from psychology and marketing, and analysed how consumer detriment can arise from market failures, regulatory failures and behavioural biases. Since they found no universally accepted definition of the term "consumer detriment", they suggested that definitions of consumer detriment fall into two broad categories, which they labelled "personal detriment" and "structural detriment". These concepts can be defined as follows:

- **Personal detriment** – negative outcomes for individual consumers, relative to some benchmark such as expectations or reasonable expectations. This may comprise both financial and non-financial detriment, with the latter including loss of time and psychological detriment;
- **Structural detriment** – loss of consumer welfare due to market failure or regulatory failure. Economists typically measure consumer welfare using the concept of consumer surplus, which is the difference between what a consumer is willing to pay for a product and what they actually has to pay.

4.4 A framework for considering consumer detriment

From these studies it became evident that the concept of consumer detriment can take many forms including high prices, missed opportunities to pay lower prices, the imposition of unfavourable sales conditions on consumers and reductions in innovation, service, quality and choice. In addition to what essentially have been identified as financial costs, it was also evident that consumer detriment can result in emotional loss.

Figure 4 below sets out the framework that we have used in this report to consider whether detriment exists in a given market, what the causes of that detriment might be and what interventions are currently in place or are planned which address the detriment.

Financial loss can come in many forms. For the retired, the most significant can be loss of income and/or capital in retirement, a position from which it is not easy for many to recover. Such events may place more individuals at risk of dependency on the state and increase the scope for society as a whole to suffer detriment. Loss of income or capital may be caused by provider default, itself triggered by criminal activity or by poor financial management and/or economic circumstances. Other types of financial loss can arise from:

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[48] Europe Economics (2007), An analysis of the issue of consumer detriment and the most appropriate methodologies to estimate it. Final Report for DG SANCO, Europe Economics, London

- Excess charges or premiums (which do not reflect the costs or risks associated with the product or service delivered often driven by lack of competition or consumer pressure in a sector);
- Failing to achieve the best returns for one's personal circumstances (typically the result of market complexity, asymmetry of information, poor standards of disclosure, lack of advice, misselling, poor levels of financial capability or consumer inertia);
- Remedial costs can be incurred where procedures for claiming for loss are not well established;
- In insurance markets, consumers can find themselves purchasing inadequate cover, or in some instances excess cover, due often to complexity and/or poor disclosure;
- The opportunity cost of not purchasing the right product can also be high. Examples include the cost of medical cover in the event of illness abroad with no travel insurance or the running out of money through failure to annuitise.

Often financial and emotional loss is connected; emotional costs are triggered by financial loss. However, it is possible for financial loss to arise without emotional consequences in circumstances where the consumer is unaware of that loss. Emotional consequences may also arise without real financial loss in exceptional circumstances. Examples might include media reports which create fear about general economic circumstances, the stability of the financial sector or about specific financial products; fears which may be unfounded or subject to existing mitigation strategies.

Figure 5: A Framework for considering Consumer Detriment in Financial Services

Type of Consumer Detriment	Causes of Consumer Detriment	Current / Planned Interventions
Financial • Capital loss • Loss of income • Sub-optimal returns • Excessively high charges / premiums / costs • Inadequate/excess cover • Remedial costs • Opportunity cost • Societal burden **Emotional / psychological** • Social exclusion • Confusion / loss of confidence • Psychological effect of breach of trust • Stress / anxiety • Health consequences • Inaction	**FS Supply Factors** • Poor value products • Lack of competition • Inappropriate risk • Complex products / excess innovation • Lack of innovation / choice • Asymmetry of information (point of sale and post-sale) • Poorly standards of disclosure • Lack of advice / limited access to sales channels • High cost advice process • Poor customer service • Inappropriate sales process • Expensive sales process • Financial mismanagement by providers • Financial exclusion **Consumer Factors** • Consumer resistance or inertia • Poor financial capability **Other** •Financial abuse • Criminal activity (e.g. scams) Legislative constraints • Regulatory restrictions • Media activity • Economic uncertainty	**Regulation** • Sales regulation • Disclosure requirements • Treating Customers Fairly • Prudential regulation **Government Initiatives** • Product legislation • Financial Inclusion • Application of behavioural economics • Deregulation / encouraging more competition **Consumer Information** • Comparative information (regulatory and market) • Information websites (Government, industry, third sector) • Financial capability • Money Guidance (MMC) **Industry developments** • Self regulation • Product and service standards **Retrospective Intervention** • Ombudsman activity • Compensation schemes • Pension Protection Fund **Other** • Third sector initiatives

Sources: OFT "Consumer Detriment under Conditions of Imperfect Information" (1997), "Focus Group Research on Consumer Detriment" (2006), "The Psychology of consumer Detriment" (2006); Marsden & Whelan (2006) "Consumer Detriment and its application in EC and UK Competition Law" (2006); FSA / Europe Economics "Firm-level Predictors of Consumer Loss through Poor Advice (2008); Authors analysis

Many of the forms of consumer detriment in financial services market have already been recognised and strategies put in place to reduce or mitigate for the loss. Strategies include a wide range of traditional legislative and regulatory tools as well as more recent moves to enhance consumer information, education and financial capability and to increase access to financial guidance. Industry moves, such as the ABI initiatives on annuities and the formation of SHIP have also sought to reduce detriment.

Among the different interventions in place to reduce and/or prevent consumer detriment in the UK, the Financial Ombudsman Service (FOS), Financial Services Compensation Scheme (FSCS) and Pension Protection Fund (PPF – discussed in section 5.1.4 below) are all well established as the final point of contact for consumers when there is a dispute with companies or when companies or pension schemes fail.

Financial Ombudsman Service (FOS)

The Financial Ombudsman Service (FOS) is an independent public body set up under the Financial Services and Markets Act 2000 to help settle individual disputes between consumers and businesses providing financial services. It will consider complaints about a wide range of financial matters; from insurance and mortgages to investments and credit. The service is free. FOS is the point of last resort for people's dissatisfaction. So the complaint of every consumer whose grievance FOS investigates will already have been through the complaints procedure of the financial businesses concerned. According to the Ombudsman this is not always the case and their research suggests that almost half of consumers who had an unresolved complaint against a financial business were deterred from pursuing it further by the fact that the business had an unhelpful approach[49]. To raise awareness of its service, FOS are targeting older people, through for example, magazines and websites aimed at the older person. They are also working with Age Concern and other third age groups to improve signposting to their service.

Businesses are now required to tell customers about the ombudsman at the start of any contract and again if an actual dispute arises. However, fewer than one in five consumers who pursued complaints in the financial year 2007/08 say they learned about the Ombudsman from the business they dealt with[50]. During 2007/08, 37% of cases were from consumers aged 55 and over (23% of all consumers were aged 65 and over). The type of complaints received are heavily influenced by the attention received in the media and though no specific age related statistics are available, anecdotal evidence indicates that complaints from older consumers are likely to relate to:

- Single premium investments – complaints usually centre around the individual feeling that the investment is too risky for them;
- Income draw-down pensions – complaints are usually around the suitability of this product;
- Pensions – problems relating to the suitability of the annuity (e.g. single/joint life, standard/impaired), delays in transferring pension funds, some administration issues).

[49] Ombudsman news, issue 76, March/April 2009

[50] Financial Ombudsman Service, (2008), Annual Review 1 April 2007 to 31 March 2008, Financial Ombudsman Service, London

Financial Services Compensation Scheme (FSCS)

The Financial Services Compensation Scheme (FSCS) is the UK's statutory fund of last resort for customers of financial services firms. It is a non-profit making independent body, created under the Financial Services and Markets Act 2000. It is funded by levies on authorised financial services firms and its service is free to consumers. The FSCS's primary role is to protect consumers against incurring financial losses when firms regulated by industry watchdog the Financial Services Authority (FSA) (and previous financial regulators) when firms are unable, or are likely to be unable, to pay claims against them relating to deposits; life and general insurance policies; investment business (on or after 28 August 1988); home finance advice and arranging, e.g. mortgage business (on or after 31 October 2004); and insurance broking (for business conducted on or after 14 January 2005. Consumers are made aware of their right to claim with FSCS press releases in the local papers.

There are limits to the amount of compensation FSCS can pay and it pays compensation only for financial loss. The rules ("COMP") governing the operation of FSCS are made by the FSA. New compensation limits will be introduced from January 2010. The current and future compensation limits are summarised in the Figure 6 below.

Figure 6: Current and future FSCS compensation limits

	Current compensation limits (2009)	Future compensation limits (from January 2010)
Deposits	100% of the first £50,000 per firm	100% of the first £50,000 per firm
Life and general insurance policies	For non compulsory insurance 100% of the first £2,000 and 90% of the balance Compulsory insurance such as motor 3rd party, 100% with no upper limit	For non compulsory insurance 90% of claim with no upper limit Compulsory insurance such as motor 3rd party, 100% with no upper limit
Investment business (on or after 28 August 1988)	100% of the first £30,000 and 90% of the next £20,000, per person, per firm	100% of the first £50,000 per person per firm
Home finance advice and arranging (on or after 31 October 2004)	100% of the first £30,000 and 90% of the next £20,000, per person, per firm	100% of the first £50,000 per person per firm

5 Consumer detriment in financial services markets

The following section examines each of the main market sectors described in section 3.7 of this report against the framework for consumer detriment described above.

We firstly describe the type of detriment that a consumer may suffer, then consider the evidence for detriment in today's market and the interventions that have already been applied to reduce the scope for detriment. We also comment on any measures of effectiveness for these interventions. The documents used to provide evidence or indicators of detriment include:

- Government reports or consultations;
- FSA thematic reviews, consultations and research papers;
- Academic research studies;
- FOS / FSCS data;
- Third sector research ;
- Consumer groups reports;
- National and trade press articles;
- Consumer and trade financial internet sites [e.g ThisisMoney, Moneysupermarket.com).

These documents have been supplemented by discussions with the stakeholders and opinion formers mentioned at the start of this report.

5.1 Decumulation – Annuities and Unsecured Pensions, DB Pensions in Payment, Equity Release

The risk of detriment in each of the decumulation market sectors differs slightly. In several, the main risks are to income in retirement whilst in others the risks are capital loss (through exposure to inappropriate risk can in turn lead to loss of future income), loss through exposure to high charges and, potentially, high remedial costs. Given the importance of decumulation vehicles in providing retirement income that cannot be replaced, any of these losses is also likely to lead to considerable emotional and psychological consequences. For society in general, the loss of income or capital in retirement can increase the burden on the public purse by increasing the number of people claiming pension credit and related benefits and potentially lead to increased healthcare costs arising from associated stress and other health issues.

In the sections below we describe the evidence that exists for potential consumer detriment in decumulation market sectors in more detail, identifying where possible the causes of detriment (in some cases, multiple) and the interventions that seek to reduce the detriment to the consumer.

The decumulation market has been perhaps the most thoroughly research of the financial markets in recent years and several research projects were in progress whilst this document was being prepared. One important feature of the decumulation market is its growing complexity. The range of products available to consumers reaching retirement is growing. Whilst this offers important choice to consumers, it also exposes consumers to the need for more advice and, potentially, to greater risk of detriment through lack of understanding of the products available.

The scope for consumer detriment is potentially exacerbated by the fact that purchasers of decumulation products have been shown to be the least well-educated groups and less well-off when compared to buyers of other financial products[51]. The same survey (CPOS) showed that:

- 'people who had already bought a decumulation product had a heavy reliance on financial advisers and did very little independent information seeking',
- unlike other markets, they did indeed tend to receive information about the products
- they had a high level of need for help in understanding products and
- even where advice was received, some struggled still to understand the product.

The survey showed that among those who had purchased a decumulation product, one in ten felt that they had bought the wrong product.

The possibility of detriment and the potential impact of poor product choices are highly significant for the group entering and in the decumulation phase. It is through this lens that we examine the decumulation market in more detail.

Many of the following issues of financial loss arising on decumulation have been widely debated and researched:

- Potential loss of flexibility or control that may arise due to constraints on the use of accumulated pension funds, in particular the requirement to annuitise at age 75.
- Whether decumulation products represent value for money or whether charges are fair.
- Whether asymmetry of information and restricted access to advice results in consumers getting the most suitable / best value product for them (e.g. protecting against inflation, taking up guaranteed rates, enhanced annuities, risk and opportunity associated with exposure to equities etc.).
- The cost of delay in transferring from a pension provider to a different annuity provider through the open market option.
- The financial stability of providers of annuities and the consequences for consumers if an annuity provider were to collapse.

Non-financial detriment may also arise where consumers are confused by the complexity of the market or confusion brought about by lack of clear information. Non-financial detriment may also arise where consumers are confused by the complexity of the market or confusion brought about by lack of clear information. Consumers may fail to act or suffer confusion or lack of confidence which in turn may lead to stress and anxiety.

[51] FSA (2008), Consumer Purchasing and Outcomes Survey (CPOS), CR76

5.1.1 Flexibility in decumulation market

The debate consumer choice in the decumulation market has gone on for many years, triggered in part by falling annuity rates and increasing longevity. A recent report published by the European Fund and Asset Managers Association[52] sought to re-open the debate. Whilst recognising the importance of annuities in protecting customers from longevity risk, they argue that better outcomes would be delivered by drawdown plans or hybrid arrangements (see section on alternatives to annuities below). Their economic modelling suggests that overall consumption in retirement is higher for most individuals in most economic conditions where individuals are exposed to equities early in retirement and gradually switch to annuities and bond holdings progressively over time. They suggest that a more gradual transfer from equities to bonds and/or annuities helps meet the consumer need for greater control over assets and the desire to bequest money during the early years of retirement, in time shifting to provide more certainty over income levels and the management of longevity risk.

Some flexibility has been introduced into the UK system in recent years. Income Drawdown has become an alternative to annuitisation (or ASP) until age 75. At present, it remains that individuals with defined contribution pension provision are required to annuitise (or purchase an ASP) by age 75. In practice most choose to annuitise at the point of retirement rather than expose their future income to any uncertainty. Some commentators consider the loss of flexibility on retirement and at age 75 caused by pension legislation to be a form of consumer detriment. Reports by the DWP / Inland Revenue[53] and the Pension Commission[54] concluded that compulsory annuitisation should remain whilst tax relief on pensions remained, although the Commission did recommend changes (and potential future changes) in the minimum and maximum age at which annuitisation could take place and products to support deferred annuitisation.

The debate continues on whether the age 75 upper limit should increase and whether complete annuitisation could be replaced by the requirement to annuitise at least up to an income level that lifted the individual out of pension credit (although it is recognised that this would add complexity, not least because pension credit levels could be a moving target. Whilst introducing more flexibility may reduce perceived or actual detriment for some, the launch of new, more complex products could in turn lead to greater detriment for others.). It is believed that the Conservative Party favour increased flexibility around annuitisation. Any increase in flexibility needs to be monitored with care to ensure that increased misselling or mis-buying, through lack of information or capability, does not arise.

Whilst considerable theoretical work has been undertaken on the benefits of flexibility in retirement, less work has been undertaken on the distribution of wealth and income in retirement. Whilst those with large funds may find that flexibility affords them greater control and improved retirement consumption, it continues to be the case that most people entering retirement have relatively small (or no) private pension provision and flexibility may be either of little or no benefit to them or expose them to inappropriate risks.

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[52] Efama (2009), Rethinking Retirement Income Strategies – How Can We Secure Better Outcomes for Future Retirees (research by Goethe University of Frankfurt)
[53] DWP / Inland Revenue (2002), Modernising Annuities
[54] Pension Commission (2005), A New Pension Settlement for the Twenty-First Century, The Second Report of the Pensions Commission

The current work on retirement income needs by the Pension Policy Institute (due for completion later in 2009), should improve our understanding of the issues facing those reaching retirement[55].

5.1.2 Traditional Annuities

Fair Pricing

Over the years, the media has often reported on the changes in annuity rates and either by design or by inference has suggested to consumers that annuities may deliver poor value for money; typically by exposing consumers to total returns that are less than the amount they use to purchase the annuity should they die early. Recent reports have focused on falling annuity rates[56], although there is no suggestion that this is for reasons other than the market driven changes to yields on gilts and bonds, most recently affected by the government's decisions on quantitative easing. Consumer research by the ABI confirms that some consumers feel that annuities do not deliver value for money[57]. Comparisons with other products are not easy due to charges being implicit in annuity rates rather than explicit, as they often are with other products.

Government departments and others have responded to concerns from consumers and the media about the value for money of annuities. A number of reports on the 'Money's Worth' of annuities have been published in recent years, examining the UK, US and other international markets. The latest UK research by the DWP[58] suggests that, overall, traditional lifetime annuities deliver fair value to consumers (rates for men aged 65 and for women aged 60 were tested). The report finds no significant difference in the value for money between men and women. Indeed, annuities appear to offer better value for money than many other financial products. The report compares the pricing of annuities with other financial products: motor and property insurance and investment products and concludes that annuities are one of the more efficient financial products available to consumers in the UK. By way of comparison, annuities attract a 'money's worth' score of around 90 (where 100 is usually as good as it gets) whilst motor and property insurance attract scores of between 40 and 60, whilst investment products attract scores of around 66% for active management and around 90% for tracker funds (with lower charges).

However, the report also finds that the money's worth of annuities may be falling slightly (2002 – 2007) suggesting that the fall in annuity rates has not directly reflected the fall in interest rates and changes in mortality expectations. The authors suggest a number of possible reasons for this:

- That regulatory costs may have increased as a result of changes to the solvency regime for insurers;
- Increased prices as insurers respond to ex-post losses on annuities;
- The adoption of a more cautious approach to mortality assumptions by insurers; a move actively encouraged by the FSA to ensure that insurers prudential position remains robust[59];

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[55] Pensions Policy Institute (2009), Retirement income and assets: do pensioners have sufficient income to meet their needs?

[56] Independent, 26th April 2009, 'Don't be rushed into an annuity deal'

[57] ABI (2004), The Pensions Annuity Market: Consumer Perceptions

[58] Cannon & Tonks (2009), Money's Worth of Pension Annuities, DWP

[59] FSA Dear CEO letter, April 2007

- The growth in the enhanced / impaired annuity market which may be deflating the overall money's worth of the annuity market – standard lives may be less fairly priced than impaired lives as a result of growth in the impaired life market.

The authors conclude that the change in money's worth is unlikely to be as a result of a lack of competition in the annuity market and that annuity rates have closely mirrored the pattern of bond yields which suggests that insurers have reflected fairly the movement in bond yields in annuity prices. However, the authors do not draw any firm conclusions as to the cause of the slight decline in fair pricing. It is useful to note however that the 2002 DWP/Inland Revenue report on Modernising Annuities did point to a lack of competition and barriers to entry to the annuity market as an issue. There is little evidence of any significant number of new entrants to the traditional annuity market, although several new entrants have launched new-style decumulation products (see below).

The continued growth of the enhanced life annuity (typically smokers) and the impaired life annuity (those with certain medical conditions) markets will reduce the level of income that others can expect from their annuity, since the pool of those remaining in the mainstream annuity market becomes more focused on those with longer life expectancy. This does not automatically imply market inefficiency but rather the growth of targeted annuity rates. The development in the use of postcodes for annuities could have a similar effect of enhancing or reducing the annuity rate depending upon where individuals live.

We have not found any research which demonstrates clearly whether smaller pension funds derive better or worse value for money than larger funds when annuitised. However, anecdotal evidence suggests that the picture on rate differentials (which may or may not be reflected in differences in value for money) is not clear cut. The size of pension pot may be considered a proxy for socio-economic group (SEG) and mortality has been shown to vary by SEG. It may be the case that different mortality assumptions are applied to those with larger funds, thus reducing the annuity such funds receive. However, this may be counterbalanced by the proportionately lower administration costs involved in dealing with larger funds. However, if this is the case, it is not necessarily an indication of market failure or detriment.

Other reports[60] confirm the overall picture of fair value in annuity markets. The paper by James and Vittas suggests value for money is best achieved in countries where long term government bonds are available to match the liabilities taken on by the insurance company. They also suggest that nominal annuities (ie those annuities where the monthly payment is level throughout) and escalating annuities (where the monthly payment increases by a fixed amount each year) deliver better value for money than indexed annuities. The explanation given for this (and supported by anecdotal evidence from insurers) is that the insurer offering indexed annuities are less well able to match their liabilities and incur higher reserving requirements. As a result, the consumer pays a higher price than they would if closer matching of assets and liabilities could be achieved. This is not an indication of market failure but says something of the mismatch between the needs of the consumer to protect the real value of their income and insurers ability to finance that need.

On a more general note about funding of annuities, the industry has recently called upon the Government to issue longevity bonds[61]. It is suggested that this would enable insurers (and pension schemes) to manage

[60] James & Vittas, Annuity Markets in Comparative Perspective, Development Research Group, World Bank
Mitchell, Poterra, Washawsky & Brown (1999), New evidence on the Money's Worth of Individual Annuities
[61] Pensions Institute (2009), Taking the Long View

longevity risk more effectively and for insurers to optimise their Solvency II position (the new European standard for insurance company solvency, due to come into effect in 2012). All other things being equal, closer matching of assets and liabilities for insurers should ensure that value for money is maintained in the annuity market.

In its 2006 report on the annuity market[62], the Pensions Institute raised concerns about the cost of advice for those with small pension funds at retirement. Commission rates for annuities are in the range of 1.3-1.5% for conventional annuities and 1.8%-2.25% for other annuities. It also questioned whether the cost of commission is factored into annuity rates for customers even where advice is not taken. At the time of writing, the current position appears unclear – we understand that some companies will offer different annuity rates for those customers not taking up the open market option (most of whom will presumably not take advice) and those who come through from other companies using the open market option. In spite of various reviews of distribution over the years, it remains the case that little progress has been made in reducing the cost of advice or widening access to advice. Whilst the Money Guidance/ Money Made Clear Pathfinder may provide greater access to generic financial advice to those approaching retirement, it remains to be seen whether the Retail Distribution Review will tackle the problem of access to advice for the mass market (see section 5.5 below).

Getting the best annuity at retirement

Much has been written about information asymmetry in the decumulation market, in particular in the annuity market because decisions are relatively complex, normally irreversible, and may have to be made in a relatively short space of time. Those who choose to defer annuitisation are generally able to switch provider and/or product type if they decide that they have made the wrong choice (although they may have lost money in the meantime). Those who purchase an annuity cannot generally change their minds later on.

Information asymmetry works both ways in the annuity market. Consumers generally have a better understanding of their own health than the insurance company (albeit that the consumer will often underestimate their longevity[63]) leading to adverse selection, particularly in the purchased life annuity (PLA) market (annuities purchased with moneys other than pension funds). This has the effect of making PLA slightly poorer value than pension annuities, although in fact rates reflect the relative risks involved for the insurer.

Most of the research into information asymmetry in the annuity market has focused on the lack of appropriate and timely information and advice for consumers from providers and intermediaries. In 2001, the Chancellor announced that the Government would consult on 'measures to improve choice and flexibility in the operation of the annuities market' whilst the FSA issued a consultation paper on information provided to pension customers on the Open Market Option. In 2002, a DWP / Inland Revenue consultative paper was published which set out a number of suggestions for improving choice at retirement and for improving consumer understanding of annuities[64]. The report highlighted the need for increased consumer education and information about annuity choices as well as the need for help or advice for

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[62] Pensions Institute (2006), Annuities and Accessibility

[63] FSA (2007), Finance in and at retirement- results of our review

[64] DWP & Inland Revenue (2002), Modernising Annuities A Consultative Document

people buying. The report also touched upon issues of flexibility and choice in the annuity market. Several initiatives, designed to improve the quality and timing of information to pension customers, were initiated in response to this debate including: an ABI Statement of Good Practice on maturing pensions; new FSA disclosure rules requiring pension firms to inform customers of their OMO rights well before maturity; the development of the FSA's comparative tables; further developments in information provision through the FSA's Money Made Clear website and The Pensions Advisory Service.

This period of change was followed in 2006 by a report by the Pensions Institute which set out a number of suggestions for empowering consumers to make rational choices[65]. This report highlighted, among other things, the very marked potential difference in outcomes for those consumers who shopped around for an annuity using the open market option and those who automatically defaulted to buying an annuity from their pension provider. It also suggested that many consumers were ill-informed about the type of annuity that they should buy (or at the very least, aware of the risks inherent in the choice they did make). This report again stressed the need for clarity of information to pension customers and proposed: highlighting rather than hiding their OMO rights in disclosure; the development of a specialist standards body for annuity providers; refinements to the FSA's comparative tables; encouragement to employers to provide advice in the workplace at retirement; the development of a level playing field between insured and occupational schemes regarding the OMO; an onus on pension companies to stress the benefits of index-linked annuities; the need for greater access to advice for those with small to medium sized pension funds.

Among the key concerns in all previous reports on the annuity market is the issue of whether consumers have sufficient information to make an informed choice about the type of annuity they purchase. This included:

- Whether those retiring get the best rate they can, either from their existing provider or through the OMO;
- Whether they make an informed choice about single or joint-life annuities;
- Whether they make an informed choice about level annuities compared to escalating annuities;
- Whether those who could benefit from impaired or enhanced annuities are aware of that option.

On the first of these points some progress has been made in recent years. Following the introduction of the FSA's disclosure rules, the ABI issued a statement of good practice to its members that set out in detail the timing, tone and content information to be provided to customers as they approach retirement or maturity. This was followed up by the FSA who were tasked by HM Treasury in tracking the operation of the OMO. In July 2008, the FSA published the findings of its thematic review[66] (undertaken as part of its TCF programme). It found that 38% of companies were continuing to use material that failed to meet the FSA's requirements and that a further 44% met only the minimum standards. Since the review, the FSA has worked with the ABI to develop templates and further guidance for firms issuing information about the OMO.

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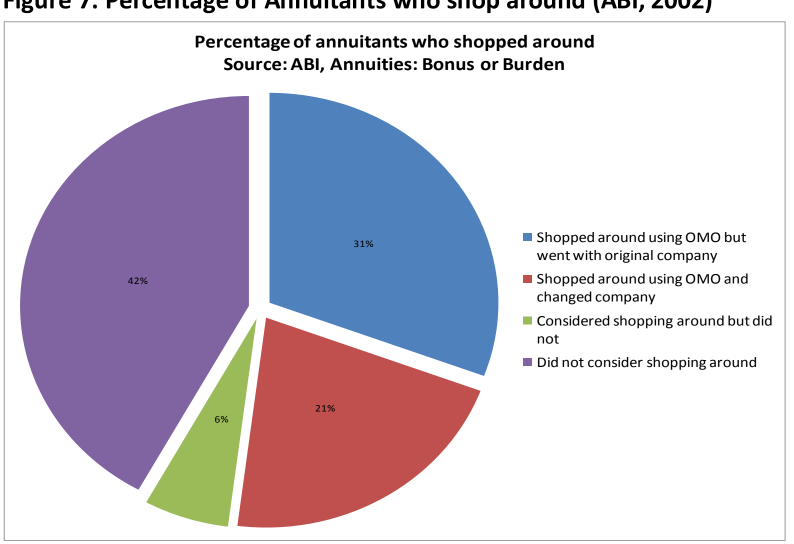
[65] Cass Business School, Pensions Institute (2006), Annuities and Accessibility

[66] FSA (2008), Results of the FSA's thematic work on Open Market Options under maturing personal pension and stakeholder pension schemes, http://www.fsa.gov.uk/pages/Library/Other_publications/Pensions/2008/omo.shtml

In spite of the developments described above, the proportion of customers using the OMO has changed little over the years. It remains about 1/3rd of consumers who reach maturity and need to make a decision on annuitisation. It is not clear however whether this level of OMO use is in fact a good indicator of consumer detriment, a fact acknowledged by HM Treasury in their 2006 report[67]. Awareness of the Open Market Option has been shown to be high (88%)[68].Consumers may choose not to exercise their open market option for a number of reasons. The HMT report pointed to evidence from the ABI of an increase in consumer awareness of the need to shop around. ABI research has shown that the picture on shopping around is not as straightforward as the OMO numbers suggest. ABI research from 2002 demonstrated this point (see Figure 7 below). Around half of all annuitants claimed to shop around. Of these, more than half stayed with their original pension company who, presumably, offered them the best rate or were very close to other rates or offered other perceived advantages to the consumer.

Figure 7: Percentage of Annuitants who shop around (ABI, 2002)



The latest research by the ABI conducted in 2008[69] estimates that 2/3rd of annuitants now shop around (up from around half in the 2002 research). 1/3rd of annuitants shop around and move provider, 1/3rd shop around and switch provider and 1/3rd do not shop around. This suggests that whilst OMO take-up may not have moved significantly, shopping around has increased from the 2002 data. This analysis is supported by a number of other research projects, including FSA estimates in 2007 based on the Consumer Purchasing Outcomes Survey[70]. It might also suggest that the requirement to encourage use of the OMO has increased competition in annuity rates; perhaps closing the gap between top and bottom companies. ABI research suggests that, for typical cases in 2007, 17 out of 23 providers offered rates to their pension customers that are within 95% of the highest equivalent rate that could be achieved on the open market). For those with small pension funds, the gain from moving to another provider may appear small. ABI data suggests that only 1/3rd of annuities are purchased with funds in excess of £35,000 and estimated that on average those

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[67] HM Treasury (2006), The Annuities Market

[68] FSA (2003), Purchasing annuities and an examination of the impact of the Open Market Option, CR22

[69] ABI (2008), Pension Annuities and the Open Market Option, ABI Research Paper No 8, 2008

[70] FSA (2007), Finance in and at Retirement – results of our review

purchasing with a fund of £35,000 the yearly gain from exercising the OMO was £128 (or 5.46%) and the lifetime gain £2,647. The gains for those with smaller funds (the majority) are smaller still. Whilst not insignificant, some with small funds may value staying with their current provider over the apparently small difference in income levels. DWP research confirmed that some annuitants stay with their provider due to satisfaction the brand and/or service[71]. Concerns about delays in payment of an annuity when using the open market option may also reduce take-up (see section on delays below).

Another reason given for low levels of OMO use is given by Dr. Ros Altman in her paper on the subject in 2002[72]. Dr Altman suggests that the very process of effecting an OMO can be off-putting for people since it involves considerably more time and effort than staying with the current pension provider. DWP research in 2008 confirms this. Whilst there has been a growth in the number of websites through which quotations can be obtained, it remains more complex than receiving a quotation for car or term insurance. The industry has yet to develop an exchange which enables the consumer to directly access quotes and then to deal directly with the provider. All business continues to be placed through IFAs. Whilst this ensures that those who do shop around tend to get advice, finding an IFA can be difficult, particularly for those who have small pension funds. Furthermore, ABI research (2008) demonstrates that fewer providers offer rates to those with small funds through the open market option.

On the issue of single v joint life, analysis by the ABI shows that 64% of annuities (by number) purchased in 2006 was single life annuities (it is not known what proportion of these are single person households). By value, 56% of annuities were joint life; suggesting that those with larger pension funds are more likely to purchase a joint-life contract – these may or may not be more affluent households. It is known (CPOS and other research) that most purchasers of annuities are currently men. Given that men remain typically older than their partners and have lower life expectancy, this strongly suggests that, in the absence of other sources of income, many female partners will suffer a significant decline in income on the death of their partner. Whilst the benefits of joint life contracts are highlighted in material sent by providers in advance of annuitisation, default quotes are normally provided on a single life basis. At the point of annuitisation, the insurer will not have sufficient information to produce an accurate joint-life quotation, specifically: whether the annuitant is single or in a couple; the age of the spouse to enable a quote to be provided.

Research has not shown adequately whether decisions on joint-life / single life annuities are made on an informed basis. It is possible that couple households place a greater value on more income now than a more sustained income for the spouse. They may also underestimate the income needs of the remaining spouse. However, some couples may have other resources on which to call. Mandatory joint life quotations or even mandated joint life contracts could reduce the detriment in later life for many women but at the cost of a higher income for the couple in earlier retirement. However, mandating such a move would prove complex and costly and could increase the detriment for some people.

The TPAS on-line annuity planner provides guidance on the type of annuity a customer may wish to purchase and the risks and benefits of each choice. The planner is explicitly designed to ensure that users understand the trade-offs they make in opting for a single life v joint life annuity or a level v escalating / index-linked annuity.

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[71] DWP (2008), Information needs at retirement: Qualitative research focusing on annuitisation decisions

[72] Ros Altman (2002), http://www.rosaltmann.com/annuityOMO.htm

The issue of level v escalating annuities is less clear cut. As noted above, index-linked annuities have been shown to be poorer value for money than level or escalating and pay out considerably less in the early years of retirement. If, as suggested by the Pension Policy Institute (PPI)[73], expenditure is generally higher during the early years of retirement, then buying a level annuity is a rational choice for many consumers. Those worried about not getting value for money from an annuity will naturally tend towards a level annuity rather than escalating. However, the PPI also suggests that expenditure rises in much later life for those with a disability or very poor health. The issue of how best to provide for long term care income needs is a difficult one that is expected to be addressed in the Government's Green Paper due to be published in the summer of 2009.

Estimates suggest that 40% of annuitants could qualify for either enhanced or impaired life annuities, with higher rates than standard annuities typically available. However, ABI data suggests that only 5%by number and 7% by value (2006 sales data) take up such annuities. Recent new entrants to the market may help push up this number as may the information available through the Open Market Option. However, what proves a benefit to some consumers is likely to reduce the level of income available to those who are not eligible as the risk pool divides.

Other recent initiatives that have sought to reduce the risk of detriment to consumers in the annuity market include a good practice guide issued to occupational DC schemes by The Pensions Regulator requiring schemes to provide information about the open market option and encouraging the provision of advice.

The most recent debate about annuity purchase comes from the Personal Account Delivery Authority (PADA)[74]. In common with many other defined contribution occupational pension schemes, the Personal Accounts will scheme not itself offer an annuity to those who use the scheme. Instead, it is proposed that PADA will offer members the opportunity to: a) to commute their fund into cash where trivial commutation rules permit and the member chooses this option; b)purchase an annuity using the open market option; c) to select an annuity provider from a panel of providers chosen by the scheme or d) to transfer their funds to an alternative pension income product. PADA will provide information and guidance (but not advice) to members on the timing and type of annuity or other products available as well as information on taking the tax-free cash sum. The proposals appear to have gained broad support from Which? and the Pension Policy Institute.

The cost of delay

Because individuals buying an annuity are often doing so at a time when their income from employment ceases, the need to replace income quickly is critical. In July 2008 the FSA published a report as part of its Treating Customers Fairly (TCF) initiative which included an examination of the detriment suffered by consumers as a result of delays caused by pension providers not paying over funds to another annuity provider when ceding payments under the Open Market Option (OMO)[75]. Their research suggested that unacceptable delays caused by the provider were occurring in 26% of the cases reviewed and a further 36%

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[73] PPI (2009), Retirement Income and assets: do pensioners have sufficient income to meet their needs.

[74] PADA (2008), Building personal accounts: securing a retirement income

[75] FSA (2008), Results of the FSA's thematic work on Open Market Options under maturing personal pension and stakeholder pension schemes, http://www.fsa.gov.uk/pages/Library/Other_publications/Pensions/2008/omo.shtml

of cases were delayed by other parties (the receiving company, the consumer or the intermediary). As a result of these findings, the ABI worked with the FSA and Origo (the industry standards body) to develop a solution. The ABI reported to us that at pilot stage transfers were taking an average of 33 days (in effect the loss of a month's income) but by May 2009 the average will be down to 7.2 days. Most large annuity providers support the Origo standard.

Missed opportunities?

Much of the focus of annuity research to date has been on the pension annuity market. However, the issues of lack of consumer awareness and understanding of annuities as well as lack of access to products apply equally in the purchased life annuity market (PLA). As a consequence consumers with lump sums to invest may never get to know about PLAs. This is particularly relevant for those taking a lump sum from their pension fund. Traditionally, many advisers would have recommended the purchase of a PLA with that money as a tax-efficient way of boosting net income (a proportion of the income from a PLA is treated as repayment of capital and is not taxable). It is evident that today, little of this type of business is written.

The PLA market is small and has been shrinking in recent years as rates fall. Commission on annuity products is typically lower than other investment products and offers IFAs no opportunity for on-going earnings in the same way as investment bonds or unit trusts. As such, annuities are a less profitable market for IFAs and consumers may miss opportunities to take a lifetime income from their investments without exposure to longevity or investment risk. Although the bequest motive will inhibit sales to many consumers, for some the product could be the most suitable use of their assets.

The debate about the appropriateness of pension annuities may also cause some individuals to delay purchasing an annuity at retirement, exposing some to inappropriate investment risk and / or the risk of falling annuity rates as longevity improves.

Counterparty Risk

Annuity purchasers have always been exposed to counterparty risk: the risk of loss of their income that could arise from the collapse of the insurer. That risk is reduced by two important interventions. The prudential regulations for life assurers are designed to prevent the collapse of a life assurer and Solvency II and the use of stochastic modelling have tightened up on the scenarios against which insurers are required to test their resources. Secondly, the Financial Services Compensation Scheme (FSCS) provides a fallback position in the event that an insurer is unable to meet its annuity obligations. The scheme provides for 90% of annuity payments to be paid by the scheme in such an event, irrespective of the annuitant's age. The scheme is therefore less generous than the PPF for those who have reached their schemes normal pension age (who under that scheme receive 100% of their retirement income) but more generous for those who have not reached normal pension age (their annuity benefits are not capped). Whilst the compensation available to annuitants provides considerable ultimate protection, an annuity provider in default would lead to considerable emotional detriment and significant, albeit short-term, financial stress.

The more critical, but less probable, risk to annuitants lies in any systemic risk arising in the financial sector or the collapse of the sector due to very significant and unexpected increases in longevity. Systemic failure would place the FSCS itself under stress in seeking to fund compensation. The FSA has highlighted concerns about the position of insurers operating in the annuity sector in its 2009 Financial Risk Outlook:

> "Longevity risk continues to be significant, and annuity providers – who are particularly subject to a concentration of longevity and credit risks – must carefully manage their risk profile." [76]

The risks are greatest for those companies exposed to higher levels of corporate bonds given the credit risk associated with such bonds and to those companies operating predominantly or exclusively in the annuity market. Firms are encouraged to consider closely their assumptions on mortality and to assume for improvements in mortality. However, as the FSA points out in the same report, there is no consensus yet on the extent to which mortality assumptions should be adjusted. Competitive pressures may result in some companies under-pricing their annuities, putting their financial stability at risk in later years. Over time, other things being equal, revised assumptions about mortality are likely to bring lower annuity rates. Whilst there is no hard evidence that companies are systematically under-pricing annuities, the issue of longevity risk and the stability of the insurance sector should and will continue to be monitored by the FSA, particularly as bio-medical research brings new advances.

Given the recent shocks to the system arising from the credit crunch, the collapse of several banks and the fall in value of many insurers' assets and the subsequent tightening up of prudential supervision by the FSA, a collapse due to systemic risk would appear to be remote. The insurance sector itself continues to fund considerable research into the issue of longevity risk, with several new papers submitted to the Institute and the Faculty of Actuaries each year as well as the on-going work of the Institute's Continuous Mortality Investigation (CMI). The CMI website acknowledges that future improvements in mortality are likely to arise from medical advances and lifestyle changes but states that the CMI does not have information available. However, individual companies, in stress-testing their assumptions on mortality, will take account of possible future changes.

One notable case of counterparty risk which has led to a tightening up of prudential regulation in the UK, is that of Equitable Life. The case is a complex one and not one for detailed debate in this report. At the heart of it the loss of a key court case combined with the provision of generous and flexible guarantees to customers, lack of access to capital markets and inadequate reserving led to Equitable not being able to meet customer's expectations[77]. Equitable entered into a compromise agreement with guaranteed annuity customers and other customers but many thousand are thought to have lost out (ThisisMoney website suggests that 60,000 annuitants have received significantly lower incomes than expected). The report by the Parliamentary and Health Service Ombudsman in 2008 found flaws in the regulatory environment and proposed compensation for some customers. To date, the Government has not accepted the findings and initiated compensation. Given the age of the annuity customers of Equitable, concerns have been raised that many will die before a decision is made and any compensation due is paid. The introduction of the FSA's Individual Capital Adequacy Framework introduced in advance of the Solvency II, is designed to prevent a repeat of Equitable Life.

5.1.3 Alternatives to traditional pension annuities

Consumers are now presented with a number of alternatives to traditional pension annuities at retirement. Some are classified as annuities (with profits and unit-linked) whilst others are classified as Unsecured

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[76] FSA (2009), Financial Risk Outlook

[77] Parliamentary and Health Service Ombudsman (2008), Equitable Life: a decade of regulatory failure

Pensions (USPs). Investment linked annuities expose customers to some equity risk and some to the potential for incomes to fall. With profit annuities typically include a guaranteed level of income whilst unit-linked annuities do not. USPs themselves can be divided into traditional income drawdown products and 'third way' products (described in section 3.7.1 above). All expose the customer to varying degrees of equity exposure. All have more explicit charging structures than traditional annuities.

Concerns about consumer detriment fall into three main categories: uncertainty about the value for money of these alternatives; uncertainty about whether consumers buying these products understand the risks to which they are exposed; concerns about counterparty risk for the consumer.

Fair pricing?

One the first of these, we have found no empirical research comparing the money's worth of annuities against the alternatives but several references to higher charges can be found, including:

- Pensions Institute (2006) reports that charges on income drawdown are typically 6% initial charge and around 1%pa annual management charges. It is thought that annual management charges may have risen since this report was written;
- FSA (2004)[78] in their reform of polarisation and the introduction of the menu show commission levels on income drawdown at more than three times the level on annuities (5.04% compared to 1.4% NPV). In their report for the FSA on the impact of commission bias, Charles Rivers Associates acknowledge that different commission levels may reflect different levels of cost in selling drawdown products[79];
- Media reports suggest that some of these products are reported to incur charges sometimes of more than 3.5% pa[80] (in part to cover the inherent guarantees).

In discussions with stakeholders for this project, the higher charges have been linked to:

- Increased product and administrative complexity;
- Higher costs of investment;
- Higher costs of guarantees / higher reserving requirements due to the volatility of underlying investments and lack of simple hedging instruments. In May 2009, an article appearing on the defaqto website pointed to two companies increasing charges due to extreme volatility in investment markets leading to higher costs of guarantees; and
- A more complex sales process involved with alternative products which leads to higher commission levels. Product providers and intermediaries incur higher sales and training costs if they sell these products.

We have found no empirical research into the costs associated with these products but anecdotal evidence suggests that companies offering these products may not all be making a profit and that the cost of

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[78] FSA (2004), Reforming Polarisation: Implementation
[79] FSA (2002), Polarisation: research into the effect of commission based remuneration on advice, Charles Rivers Associates
[80] Sunday Times 26th October 2008, Your 10 point guide to unravelling annuities

delivering guarantees could be undermining profitability in the current climate. There are also suggestions that customers of such products may be worse off than purchasing a straightforward annuity in volatile markets.

Information asymmetry / misselling

Many of these products relatively new to the UK and remains a small part of the decumulation market. Information asymmetry lies at the heart of concerns. Whether consumers understand the risks that they are taking in using drawdown plans or other unsecured pensions is unclear. Ill-informed decisions could lead to psychological stress and unexpected financial stress as a result of stock market performance.

In the current economic environment, almost all income drawdown investors are likely to have seen significant falls in the value of their funds and a consequent fall in income. Whilst writing this report, the trade press started to highlight the potential for an increase in misselling claims as misselling claims firms start to target the drawdown sector[81]. The article pointed to a 50% increase in FOS cases relating to income drawdown in 2007/08, albeit from a very low base (88% in 2006/07). A related article 'Drawdown dangers' published by Money Marketing in May 2009 highlighted the risks associated with drawdown, particularly when drawing income at a time of falling stock markets. In an earlier article in February 2008, the Telegraph newspaper warned of the similarities between the products being launched in the UK and those which have been subject to misselling cases in the US[82]. The same report questions whether clients who are paying high charges for the guarantees built in to these products are likely to see any returns.

We have found no detailed research into consumer understanding of these products, although the FSA suggests that understanding of decumulation products in general is low[83]. The FSA has also highlighted the risks of consumer detriment in the income drawdown market. In its Financial Risk Outlook report of 2005, it set out its concerns that changes to pension legislation could lead to more consumers buying income drawdown products and being exposed to unexpected falls in income as a result of poor investment performance and later changes in annuity rates. They stress the importance of high quality initial and on-going advice.

The title of a recent web article highlights the difficulties with some of these products: *"Are variable annuities just too scary for advisers?"[84].* The article goes on to quote an individual from Legal & General who suggests that the products are 'quite complicated and expensive... Many IFAs will be very careful about advising on these things'. Whilst reassuring that advisers are careful about advising on such products, this level of complexity might suggest that consumers will find it even harder to comprehend them fully. In the US, variable annuities (upon which some UK products are based) have been the subject of considerable misselling claims and compensation[85]. Whilst the products offered in the US are different to those on offer in the UK, the UK market may still need to be alert to the potential for misselling, particularly where

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[81] Money Marketing 21st May 2009, 'Claims chasers on the trail of drawdown'
[82] Telegraph.co.uk (2008), Clouds gather over US-Style annuities
[83] FSA (2007), Finance in and at retirement – results of our review
[84] www.citywire.co.uk, April 2008
[85] http://www.telegraph.co.uk/finance/personalfinance/pensions/2784848/Clouds-gather-over-US-style-annuities.html

commission levels for such products are higher and levels of sales of many other products are in decline in the current economic climate.

With any alternative to a traditional annuity, there remains no guarantee that income received at age 75 will be higher than could have been purchased at younger age. If funds shrink in value and/or mortality assumptions move against the consumer, the benefit of buying an annuity at an older age (and a higher rate than younger ages) could be negated.

Counterparty Risk

In their paper for the Staple Inn Actuarial Society[86] and in subsequent presentations, Abbey and Henshall suggest that some of the problems encountered in the US market can be accounted for by a failure of insurers to account fully for the risks associated with variable annuities and a failure to understand consumer behaviour. The authors go on to suggest that UK companies are better positioned to understand and account for the risks of 'third way' products and that the introduction of the concept of economic capital as well as stochastic and 'least solvent likely event' modelling should help providers ensure that they hold adequate capital.

Whilst the level of compensation available to traditional annuitants is high, the level of compensation available to those investing in alternative products may be considerably lower, and for some potentially as low as £50,000. For those with hybrid products, the level of compensation is not entirely clear.

5.1.4 DB Pensions in Payment

The closure and some high profile collapses of DB pension schemes have made this part of the market headline news in recent years. DB pensioners and those approaching retirement have historically been at risk of losing all or a significant proportion of their pension income in the event of the collapse of a scheme due either to the collapse of the employer sponsor, fraud (as in the case of Maxwell) or a weakening of the employer covenant. Since the Maxwell case, the UK rules on the governance and prudential regulation of pension schemes has been tightened through successive legislation, increased powers for The Pension Regulator (TPR) and the introduction of the Pension Protection Fun (PPF).

The problems that lie behind the sustainability of DB schemes are well documented. They centre on lack of funding, uncertainties about longevity, increased costs of administration, increased transparency of liabilities, concerns about employers commitment to DB schemes and market volatility, and all remain highly relevant and topical issues. Recent headlines have generally not painted a rosy picture:

"Consultants expect new wave of scheme closure"

"Number of FTSE 100 firms at 'material risk' from schemes doubles"

""Worried trustees assess employer covenant" [87]

However, just to show how uncertain the position is, in April 2009, FT.com published an article highlighting the fall in DB scheme deficits[88] and consultants Pinsent Masons published a report suggesting the 'DB is not yet dead'[89].

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[86] Abbey,T & Henshall, C (2007), Variable Annuities, Presented to the Staple Inn Actuarial Society 16th October 20087

[87] Professional pensions website, April & May 2009

The requirements placed upon employers to fund DB schemes adequately have been tightened significantly as have the responsibilities and powers of the trustees of schemes. The Pensions Act 2004 has led to trustees negotiating recovery plans with employers in situations where funding is deemed inadequate. The same legislation extended the protection available to members in the event of a winding up of the scheme.

Inevitably the subject of longevity risk in DB schemes is returned to regularly. In its second report, the Pensions Commission[90] studied the subject of the Government's issue of longevity bonds to help secure DB schemes. It concluded that the state is already subject to excess longevity risk and that it should not expand that risk by the issue of bonds. However, the subject has returned and a recent paper issued by the Pensions Institute[91] suggested that Government issued longevity bonds would help sustain both DB schemes and the growth in insurance company annuity business. In the absence of such bonds, and as an alternative to winding up schemes, at least two companies, The Pension Corporation and Aegon, have entered the longevity insurance market. They both offer DB schemes insurance solutions which help the scheme to continue, albeit perhaps closed to new entrants.

Whilst the closure of schemes to new entrants and future accruals affects future generations of the retired rather than today's, a withdrawal of the employer covenant and the winding up of a scheme can lead to worry and stress among pensioner members of schemes. The key concerns or risks to pensioner members are

- Having their pension payments 'bought-out' by an insurance provider;
- The insolvency of the employer leading to the pension scheme being in default. In such cases (where insolvency occurs after April 2005 and the winding up of the scheme has not started before that date), the PPF should step in.

Whilst the transfer of pension payments to an insurer may lead to some concern, annuitants receive protection under the FSCS broadly equivalent to their protection from the PPF. Moreover, detailed rules apply to such transfers to ensure that incomes and commitments are maintained and the TPR oversees such activities. Members may still have some concerns about the loss of discretionary benefits available under DB schemes in the event of a buy-out. Legislation and supervision by TPR have been put in place to reduce the potential for consumer detriment among members of workplace pension schemes. TPR's current (expanded) powers were set out in the Pensions Act 2004.

The insolvency of an employer and insufficient assets in the pension scheme to wind it up should in many cases lead to the PPF stepping in to protect scheme members. Since 2005, members of DB schemes have been afforded some protection if the scheme qualifies for PPF protection. Members of schemes which collapsed before 2005 have suffered very significant losses to current or future income. Schemes that collapsed before 2005 were subject to a priority order in which accrued benefits were paid. Many members might not receive their full benefits and some might receive nothing. In the current economic climate, funds continue to call upon the PPF In the event of the collapse of a DB scheme, a hierarchy of protection

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[88] FT.com (13th May 2009), 'UK company pension deficits fall in April'

[89] Professional Pensions (19th May 2009), http://www.professionalpensions.com/857959

[90] Pensions Commission (2005), A New Pension Settlement for the Twenty-First Century, The Second Report of the Pensions Commission

[91] Pensions Institute (2009), Taking the Long View

unfolds. Members of schemes that have reached their schemes normal pension age, those in receipt of a survivor's pension or who have retired through ill-health will continue to receive 100% of their pension payments. Those who have not yet retired or who have retired before the normal pension age will receive 90% of their pension payments (current or future), subject to an actuarially calculated cap that depends upon a number of factors including the age of the member when payments become due[92]. The PPF has just announced that the cap for 2009/10 is £31,936.32 for a person aged 65 (and not yet retired and in receipt of their pension. The cap will be different for different ages. For some of those who may have retired or partially retired but are not yet in receipt of their DB pension, the cap may represent a reduced level of income in retirement from that expected.

Ever since its formation, concerns have been raised about the sustainability of the PPF; concerns that have increased in the current economic climate. As more schemes are transferred to the PPF, the burden on those remaining schemes (who fund the PPF) grows, thus exacerbating the situation. If more and more DB schemes are wound up (of are transferred to the PPF), there will ultimately be very few schemes left to fund the PPF. At present, there appears to be no answer to what happens in the event of such circumstances. In 2007, the PPF issued a paper discussing the long-term risk to the PPF. The model illustrates the low number of scenarios which could result in an extremely high level of claims on the PPF. The scenarios also suggest that in most cases, the fund will have a surplus but that in one in ten cases the fund out have a significant deficit (£2.6bn or more). Current economic conditions appear to be close to some of the more downbeat scenarios modelled. The PPF has just taken on its 100th scheme and some large schemes are starting to be named as at risk of joining the PPF ranks. The collapse of large employers with large schemes increases the chances of a large deficit at the PPF. At present, there appears to be no answer to what happens in the event that the PPF is unable to meet its liabilities.

5.1.5 Equity Release

Like annuities, the equity release market has been the subject of considerable research. Major studies or reports have been issued by:

- The Institute of Actuaries in 2001 and 2005[93];
- A series of papers from the Joseph Rowntree Foundation (JRF);
- A 10 year retrospective by Norwich Union published in 2008[94];
- Various reviews of the market by the FSA, both in advance of and following regulation of the market;
- On-going research by the Resolution Foundation[95];
- A review of the market by Peter Williams for the Council of Mortgage Lenders (CML) in 2008[96];

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[92] PPF (2009), How is compensation calculated,
http://www.ppfonline.org.uk/ppf/pdf/PPF_factsheet_compensation%20calculated.pdf
[93] Institute of Actuaries (2001), Report on Equity Release Mechanisms; (2005), Equity Release Report;
[94] Norwich Union (2008), Equity Release, Yesterday, Today, and Tomorrow
[95] Resolution Foundation (2009), Accessing Housing Wealth
[96] CML (2008), Please Release Me.

- A report by Watson Wyatt for the Panel in 2006[97].

In addition, SHIP is in the process of developing a policy paper on the future of the equity release market.

The risks to the consumer from this market are similar to those in other decumulation markets; namely the risk to capital (equity) and income; the risk of inappropriate pricing; lack of access to the market or lack of access to appropriate advice; emotional stress brought on by the purchase of an inappropriate product or stress caused by media reported market failures.

Fair pricing

During this research, we continued to hear anecdotal references to the poor value that equity release represents. However, those making these comments acknowledged that the remarks were made in relation to the relative costs of equity release compared to traditional mortgage rates. The economics of equity release products vary considerably from traditional mortgages, not least because providers tend not to receive any income from the asset they hold until the death of the customer and in many cases the provider is taking on the negative equity risk. The report prepared for the Panel in 2006 suggested that levels of profitability in the lifetime mortgage market are not extreme, particularly where the risks of negative equity and mismatching are taken into account. The report by Peter Williams for the CML confirms that a number of factors contribute to higher rates for equity release. Furthermore, the FSA itself refers to data collected by SHIP which it suggests shows that price competition is effective in the equity release market. There would appear to be valid commercial justification for interest rate or pricing differentials between equity release and standard mortgages.

Concerns about transfer costs (to another provider) are also raised by market commentators but these are also common with traditional mortgages and can be commercially justified.

Getting the right product

The market for equity release is complex with many different products available with different levels of risk. The history of equity release is littered with examples of consumers buying products for which they did not understand the risks – in particular the Home Income Plans of the 1980s. Many claims for misselling of these early products have resulted in compensation being paid. Since then consumer awareness of the risks of equity release has almost certainly improved (although we have no empirical data to support this claim) and the media monitors the market closely for the consumer. The types of risk encountered by the early customers of equity release, some of which have been reduced through interventions, included:

- The risk of negative equity. The roll up of interest in a lifetime mortgage combined with a long life could lead to negative equity and the estate of the individual having to repay that sum. Many providers now have a negative equity clause in their contracts;
- Inflexible contracts which prevented the individual from moving house, repaying the funds or transferring to another provider. The market has advanced significantly in recent years with greater flexibility built in. However, products do still vary and consumers need to assess the features of products carefully before purchase;

[97] Financial Services Consumer Panel (2006), Report on the value of equity release products to UK consumers

- That in the event of default by the provider, their plan would remain in place and they would not have to repay their mortgage or otherwise put their home at risk.

Many of these risks have been addressed by the industry through the formation of the industry body SHIP, which require members to provide lifetime right of tenure, a no negative equity guarantee, the freedom to move home without penalty and certification of independent legal advice. However, variations still exist in product terms across the industry.

Perhaps the most significant shift in the market for equity release came with the introduction of mandatory regulation of advice by the FSA. The FSA put in place detailed rules for disclosure, the sales process and training and competence requirements, initially for lifetime mortgages and subsequently for reversion mortgages. The industry has responded by developing specialist qualifications for those seeking to give advice in this sector. Most recently the sale of 'Sale and rent back' products has also come under review by HM Treasury[98], FSA[99] and OFT[100] following widespread criticism of the products and associated sales practices. The OFT report recommended that the sale of such products become subject to FSA regulation, potentially bringing them into line with the competing products. Age Concern has expressed support for the proposals. HM Treasury and FSA are currently consulting on this approach.

In spite of changes in the products designed to protect consumers, the FSA continued to identify cases of misselling well beyond the introduction of sales regulation. As recently as November 2008, the FSA warned mortgage intermediaries of the risks of moving into the equity release market and the potential risk of misselling[101]. Which? also continues to monitor the latter is due to publish a report on the subject in the near future. In certain cases, consumers who are missold products can seek redress through the complaint system and FOS or in more extreme cases through the FSCS. In 2007/08 only 35 claims were received by the FSCS relating to the whole mortgage advice sector.

One further source of detriment concerns access to the market, particularly for those with lower value houses or less equity. Until recent years, very few major brands operated in the market and those that do now typically restrict access to the market to those with significant levels of equity in their homes. JRF has called for local authorities to get more actively involved in the equity release market to provide access to those who wish or need to release small sums and others who would not be catered for by the commercial market. To date, the response is believed to have been varied across local authorities.

Access to appropriate advice can also be a barrier to finding the best product or gaining access to the market at all. Sales of equity release are, in the main, controlled by the IFA channel. Whilst more IFAs now have an appropriate qualification in equity release and more have experience of the market, it remains the case that IFAs in general are becoming more focused on the higher income and wealth segments of the market, thus withdrawing advice from the mass market. Whilst the FSA's Retail Distribution Review (RDR) sought to address the wider advice gap, clear ways forward and industry solutions appear to be several years away.

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[98] HM Treasury (2009), Regulating the sale and rent back market: a consultation

[99] FSA (2009), Regulating sale and rent back: an interim regime

[100] OFT (2008), Sale and rent back: An OFT market study

[101] FSA (2008). The challenges facing the mortgage intermediary sector. Speech by Lesley Titcomb, Director of Small Firms and Contact Centre, FSA

Counterparty risk

Consumers with equity release mortgage products face much the same risks as other mortgage customers in the event of the default of a provider. Recent history has suggested that the Government may step in where a bank is in default and take over, albeit temporarily, the running of the mortgage book. Otherwise, the mortgage book may be sold as part of the assets of the company to another provider.

5.1.6 Summary

Decumulation

The very importance of the decumulation market to those entering and in retirement combined with the complexity of the market make for one where consumer detriment is both feasible and significant. Many different interventions have been put in place to protect the consumer, and to a large extent markets are thought to operate efficiently. Overall, there is little evidence in any decumulation markets of poor value for money products, with competition working to limit charges. However, there remain widespread perceptions of poor value for money and some gaps in empirical evidence, in particular around alternatives to traditional annuities.

A number of initiatives in the market have sought to reduce the asymmetry of information, most recently in developments in the annuity market. However, consumer understanding remains low and the scope for misselling or misbuying high. FSA sales regulations limit the volume of misselling but where it does occur the consequences for the consumer can be severe, extremely stressful and in some cases difficult to remedy.

Consumers are protected against default by insurance companies and pension funds, although in the case of some products (income drawdown for example), the protection is limited to £50,000. Protection for those with annuities is close to 100%, for as long as insurance companies continue to be able to fund the FSCS. The level of protection afforded those with hybrid products is not clear and may require clarification. There are no indications of risk of their failure to do so but major improvements in mortality could present the industry with challenges. Those in DB schemes in default are protected (some up to a cap) as long as there are sufficient DB pension schemes to fund the PPF. There exist some concerns about the long-term sustainability of the PPF.

In section 0 of this report we summarise for each decumulation market where we consider the hotspots for consumer detriment to exist.

5.2 Protection - Life, Health, Travel, Motor and home insurance

Current thinking on the risk of detriment in these product markets is dominated by the view that age discrimination is a key factor in the ability of older people to obtain appropriate insurance cover. The exception to this is home insurance, where availability and rates are generally considered to meet the risk profile and needs of older consumers. Where detriment in the protection market is felt to occur, the main risks are considered to arise from lack of access to the appropriate or needed product and the subsequent emotional/psychological effects arising from this rather than from cost. In many instances, however, a financial cost is likely to arise due to higher premiums, where cover can be obtained. Age Concern and Help the Aged[102] acknowledge that higher premiums are appropriate to reflect the increased risk presented by older consumers. However, they believe that the use of seemingly arbitrary age thresholds such as 75 or 80 lead to "unreasonable and disproportionate" increases in premiums. Among many older consumers, these significant increases are viewed as unfair.

In the sections below we describe the evidence that exists for potential consumer detriment in the protection market sectors in more detail, identifying where possible the causes of detriment (in some cases, multiple) and the interventions that seek to reduce the detriment to the consumer and remark on the perceived effectiveness of such interventions.

In their impact assessment report, the Government Equalities Office[103] notes that age sector organisations suggest that by removing minimum and maximum age limits, older customers would save £4.5m annually in search costs, and that £131m to £1,180m of consumer detriment would be removed for those over 65 in motor and travel insurance alone. In contrast, financial services representatives estimate that, rather than reducing costs to the consumer, the removal of minimum and maximum age limits in motor and travel insurance would add around £482m in the first year with diminishing ongoing costs. The industry also estimates that for the long-term insurance sector (life assurance, long-term care insurance, longevity insurance, annuities), one-off costs could be at least £275m with ongoing costs of £105m per year. The Working Group sought broad qualitative and quantitative estimates from only a small sample of representative firms, and as such the results are subject to important caveats and must be treated with caution[104].

Unlike many decumulation products, most protection products for those in later life are a continuation of, or very similar to, products used in earlier life. Familiarity, and to some extent the discretionary nature of the products, may serve to reduce the potential for detriment.

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[102] Age Concern and Help the Aged (2008), Increasing access to insurance for older people: some questions and answers,

[103] Government Equalities Office (2009) , Equality Bill - Impact Assessment, TSO, London

[104] Government Equalities Office (2009) Equality Bill Impact Assessment

5.2.1 Life insurance and Funeral Plans

The main risks of detriment arising from life insurance and funeral plans that consumers face arise where: the premiums paid exceed the value of the plan; inadequate cover, for example the sum assured does not cover the cost of a funeral; reduced inheritance arising due to a lack of advice and/or financial reviews.

Life insurance

Various forms of life insurance for older people exist. Some take the form of traditional life (term) assurance requiring a medical history, others offer whole of life insurance, again with some medical history questions while a third option (usually described as 'over 50 plans') does not require medical questions but will have higher premiums as a result. For each of these plans, providers often promote that they can be used to contribute to funeral expenses. The main areas where consumer detriment could arise include:

- For term assurance and whole of life plans, the policy payout may be subject to inheritance tax unless the plan is put in trust;
- If term assurance is used for funeral planning, consumers may risk 'wasting' their premiums if they outlive the term of the contract;
- Though whole of life insurance has no policy expiry date, consumers might pay more in premiums than the policy could pay out on death, particularly where the provider requires premiums to be paid for as long as the policyholder lives. Some providers will continue to provider cover but will stop collecting premiums at, for example, age 80;
- Typically, over 50 plans only offer full cover after 18 months or two years, though a proportion of the premiums made are paid out if death occurs within this period. Generally these plans are most cost effective for older people if their medical history makes other forms of life cover expensive or obtainable.

As with all life assurance, premiums relate to age and health (where a medical history is required), a factor which is widely accepted as a good proxy for risk in this market as the probability of death increases with age[105]. In this market the maximum age for life cover can vary among providers. Some providers are now increasing the maximum age and industry commentary indicates that this is expected to continue[106].

Regulatory interventions are in place to protect the consumer. Life insurance buyers are exposed to counterparty risk: the risk of loss of cover if their insurer collapsed. That risk is reduced by two important interventions, the prudential regulations for life assurers including Solvency II and the FSCS. The impact of these interventions are covered in detail in section 5.1, decumulation.

Funeral plans

Funeral plans may be either an insured funeral expenses product (structured as a whole of life product) or a pre-paid funeral plan (typically taken out with a funeral director). In recent years the insured funeral plan

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[105] Stakeholder interview 29 April 2009, Equality Bill (2009), Volume II, TSO, London, ABI (2009), Age and Insurance: Helping older customers find the cover they need

[106] AXA increases life cover age limit to 85 and period before declaration of health to 180 days, AXA press release, 16 February 2009, www.axa.co.uk/media/pressreleases/2009/pr20090216.html, Stakeholder interviews 16 April to 20 May 2009

market has been growing and is estimated to have increased by 20%-30% over the past year[107]. Premiums are typically low and plans do not usually require any medical evidence. This simplifies the sales process and enables many older people to get low level life cover with ease. However, anecdotal comments highlighted that concerns have been raised in the past about the charges inherent in such products[108]. As a whole of life contract, it is possible for the customer to live long enough that they pay more in premiums than will be paid out in sum assured (see life insurance above). Buyers of these products may also not be aware that such products may not cover the costs of a basic funeral. In the last two decades, the cost of the average funeral has risen sharply. Figures from Mintel's Funeral Business Reports show that from 1988 to 2006, the increase in the average funeral cost had exceeded the rate of inflation[109]. However, stakeholders interviewed tended to feel that it is a relatively transparent product that meets an identified need and that the market works well.

Statistics from the Funeral Planning Authority (FPA) show that the pre-paid market is growing at approximately 11% per annum with almost 75,000 new plans taken out in 2008 with their registered providers. Pre-paid funeral plans are usually sold by funeral directors who pay the funds into a trust or a client account to ensure that they funds are available when required. They are not FSA regulated products. Instead they are regulated by the FPA [110] which since 2002 is the self-regulatory organisation for the UK Funeral Planning sector. They also provide a conciliation service to resolve complaints and disputes that might arise. Not all companies selling funeral plans (as legally defined) are registered with the FPA[111] nor are they obliged to do so. Potential detriment could arise if the plan was taken with a non FPA registered provider and the funeral firm became insolvent, is taken over or the funds were misused. In this situation in addition to the financial loss; stress and anxiety may also be caused to the affected individuals and/or their family, who will worry about having their funeral paid for. Though few instances of this occurring have been found in the press, the most recent incident was reported in the Manchester Evening Post in March 2009[112]. This report illustrates that although regulation protection is in place, it does not offer complete protection against misuse of funds. Pre-payment funeral plans can also work to the advantage of the consumer if funeral costs rise faster than investment returns on the pre-payment made. In such circumstances the final cost of the funeral could be higher than the pre-payment made, depending on how long the individual lives after taking out the plan.

5.2.2 Long Term Care (LTC) Insurance / Immediate need annuities

Long term care needs are either met by the State and/or long term care insurance, immediate needs annuities or, increasingly, individuals' income or savings.

Ultimately, the provision of state support for care needs for those with very limited resources reduces the detriment suffered by individuals in funding long-term care. However, the complex interaction between

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[107] Stakeholder interview 29 April 2009

[108] Stakeholder interview 29 April 2009

[109] Mintel (2007), Funerals

[110] The detail of regulation of funeral plans is contained in articles 59 & 60 of The Financial Services & Markets Act 2000 (Regulated Activities) Order 2001, www.legisation.hmso.gov.uk/si/si2001/20010544.htm

[111] Article 59 of The Financial Services & Markets Act 2000 (Regulated Activities) Order 2001, www.legisation.hmso.gov.uk/si/si2001/20010544.htm

[112] http://www.manchestereveningnews.co.uk/news/s/1105111_funeral_firms_trail_of_misery

state funding, benefits and private provision, the distressing nature of decisions about long-term care and the lack of consumer understanding of the system, combine to make emotional detriment both material and likely for many. Decisions which involve financial transactions can also lead to financial detriment where inappropriate products are sold or purchased.

Government provision

The NHS is legally obliged to provide long term care funding where an individual requires specialist supervision or equipment. In order to be eligible for fully funded NHS care (ie the cost of both health and social (personal) care) a person will usually need to have a high level of care needs. If an individual does not qualify for fully funded NHS care but is assessed as having nursing care needs, these will be met by the NHS and their social care funding will be provided by the local authority subject to means testing.

Social Services must assess each applicant in relation to their needs for domiciliary or residential care. If a need is determined, they will the assess whether the local authority or the individual themselves should pay for the care required. As of April 2009, if an older person in need of care has £23,000 or more in income and capital (£22,000 if they live in Wales, £22,000 in Scotland), they are assessed as being able to meet the full cost of their care. If capital and income are worth £14,000 or less, the sum is disregarded and local authorities will cover the cost of providing care. If capital and income are between £14,000 and £23,000, an assessment is made of what the individual can afford to pay.

The local authority may choose not to count the home as capital if the carer lives there but it is not obliged to do so. Councils can assist with the funding of care home fees for the first 12 weeks of care. Beyond that they can enter into deferred payment agreements, where funding is charged against the value of the property, until the death of the individual in care[113]. Councils also have the discretion to offer financial assistance in certain cases, but rarely have the resources to do so. In early 2009, Channel 4 News found that many authorities do not exercise these additional options[114].

Against this background, consumers traditionally have had an expectation that the State will provide. Though this has been declining in recent years, the London School of Economics found in 2008 that almost one third of adults polled believed that care would be free for them in the future, despite widespread means testing and eligibility thresholds.

Following the Wanless report 'Securing Good Care for Older People' in 2006, the government committed to long term reform of adult social care funding in October 2007. After a period of extensive consultation, the government has confirmed that the Green Paper on care and support reform for England will be published in June 2009. The government is considering a number of options to improve the system in terms of both funding and delivery of services, some of which might include the private sector.

[113] http://www.dh.gov.uk/en/SocialCare/Chargingandassessment/ChargingforSocialCare/DH_079505

[114] http://www.channel4.com/news/articles/society/health/care%20funding%20postcode%20lottery/2913787

Long term care insurance

From the commercial perspective, lack of consumer demand coupled with little government incentive has limited development of insurance and/or other financial products to meet the payment of long term care services, even though the cost of long-term care is predicted to double in the next 20 years[115].

The market for pre-funded long term care insurance (LTC) is largely dead as there are now no providers offering pre-funded insurance. Stakeholder interviews confirmed that the reasons for the collapse of the market include the inability of the market to construct products that were attractive to the consumer and the higher regulatory costs incurred as a result of FSA classification of LTC insurance as a complex product requiring specialist advice. Consumer reluctance to buy the product has also contributed to a lack of interest in LTC. FSA research has found that consumers prefer to risk losing their house, than spend a substantial amount of money on an insurance policy that may not be needed[116].

In the absence of a LTC insurance market, one of the main ways in which homeowners can pay for care (among those with limited or no savings or investments) is through releasing equity in the home to pay for on-going care costs (see earlier section on Equity Release). Alternatively, people may choose to sell their home if going into residential care. The current economic environment means that people might find it difficult to do this and therefore they might resort to using a bridging loan, such as those offered by BridgeFast, an independent property sales management and funding company, authorised and regulated by the FSA. In one of the stakeholder interviews conducted for this report, concern was raised about this option as it was thought that bridging loans did not offer value for money to what are potentially vulnerable customers.

Immediate needs annuities

The immediate needs annuity market is small with only two firms (AXA and Partnership) offering products. An immediate needs annuity will pay all or part of the fees until the person in care dies. Variations on the product are available such as escalation rates, capital protection and deferment. The annuity is paid directly to the care provider and is tax free. The main form of detriment to the consumer is likely to come from a lack of supply and a lack of competition in this sector of the market. However, we have found no evidence of poor-value pricing.

5.2.3 Longevity Insurance

Aside from the protection from excess longevity afforded by the annuity market and the 'no negative equity' terms in the equity release market, there are currently no products available on the market in the UK to protect individuals from living too long and running out of funds. Until 2008, a policy was available from LifeTrust, an Irish life company operating in the UK. The Life Trust Longevity Plan was a single investment plan that aimed to provide a rising income for 20 years from age 75 or 80 for those still living as other policyholders die. Money had to be invested for a minimum number of ten years before the plans began to pay an income. For tax purposes, the plan was treated as a purchased life annuity. In 2008, the company closed its doors due to the high cost of delivering guarantees; another indicator of the uncertainty and lack of financing opportunities for insuring against longevity.

[115] Saga (2008) Saga Cost of Care Report 2008/2009
[116] FSA (2002) The impact of an aging population on the FSA

5.2.4 Income protection

There is the potential for further change in this market as people will have to work longer. Most companies will cover an individual up to 65 years and some companies will now insure someone up to 70 years of age. No evidence has been found to indicate that there is a market for income protection beyond 70 years of age. Within this context, consumer detriment does not appear to be an issue.

5.2.5 Health insurance

A few firms specialise in providing cover to older people and many insurers will extend cover to those leaving corporate schemes. However, the majority of older people do not have private health cover.

The Experts' Working Group report on age discrimination in financial services expressed the view that older customers are well served and that there are few complaints of age discrimination, although customers might find steep increases in premium occurring when they move from one age band to another. Age is a factor used to determine the level of premium to be paid and this is determined by actuarial data. No research or commentary has been found to contradict the view of the Experts' Working Group that this market where little premium detriment exists.

However, there are some concerns about whether older consumers understand that some policies exclude pre-existing medical conditions from cover and that, as a result, they may not be covered for those conditions. Information asymmetry may exist in cases where it is not clear to the consumer what the exclusions from a policy mean in practce, particularly those relating to pre-existing conditions.

5.2.6 Travel insurance

In the travel insurance market, research and debate has focused on the extent to which age is a suitable proxy for risk and on the availability of travel insurance for older people. The use of age as a discriminator is considered to result in higher premiums for older people and lead to people unable to obtain travel insurance. According to the ABI, age is only one factor used in determining the level of premium to be paid and that people are more likely to have difficulty in getting (affordable) cover due to health issues rather than age. Nevertheless there is a public perception that it is age rather than health which determines the level of premium paid and that individuals are refused cover because of their age. It is worth noting though that Age Concern research found that most respondents thought that their travel insurance offered at least 'fairly good value'.

Age Concern and Help the Aged research finds that older consumers report difficulty in obtaining travel insurance with 29% of the attempts made by those aged 75 and over failing to obtain a quotation for insurance[117] . In contrast, ABI research finds that more than 98% of customers aged 65 or over are able to find travel cover, although 25% are turned down by at least one insurer (often for health reasons rather than age).[118] April 2009 data from Defaqto demonstrates that older people should be able to find travel insurance cover as there are 18 firms with no upper age limits for annual travel insurance and 19 firms with no upper age limits for single travel insurance. This data supports the ABI view[119] that age limits in the

[117] Age Concern and Help the Aged (2007), Insurance and Age: exploring behaviour, attitudes and discrimination, ACE, London

[118] CRA International(2009) Insurance and Age-based Differentiation, ABI Research Paper No.12

[119] Stakeholder interview, 23 April 2009

travel insurance market are increasing. In 2007 the ABI[120] reported that 63% of travel insurance companies had an upper age limit on single trip policies, and annual policy age limits were, on average, 72 years.

Within the travel insurance market, some consumer detriment may arise where individuals pay higher premiums coupled to exclusions than is perhaps necessary for their needs. Surveys of the travel market by Age Concern and the Equality Commission for Northern Ireland have found a wide variety of quotations from different providers for the same trip, for example, annual travel insurance for an 80 year old could range from £94.95 to £210.90. Significant differences in the premiums quoted within provider by age were also found, for example, premiums for a 14 day single trip could cost £18.49 for those aged 65-69 years and £35.51 for someone aged 75-79 years. Concerns about the wide variations in the treatment of those with physical limitations/illness in this research have also been expressed by Age Concern. They also found that the most competitive quotes are generally only available through the internet, which is not accessible by many older people. In order to obtain the best deal, older people will need to shop around and yet FSA research has found that older people do not tend to shop around as much as younger people for general insurance[121].

While older people may experience some financial detriment through higher premiums being charged, Age Concern and Help the Aged research finds that the potential for emotional detriment is likely to be higher. If older people are unable to afford or obtain travel insurance their social well being may be affected as they are unable to live a more active lifestyle or be unable to visit family overseas. They found that some older people have been put off travelling due either to the difficulty of accessing insurance, cost of insurance or fears about the cost of insurance. In some instances, people may choose to travel without cover in the hope that it will not be needed. Others may decide not to declare a medical condition when taking out the policy in order to control costs.

Existing interventions such as the FSA's financial capability initiative and Money Made Clear information source provide limited assistance in helping the individual determine where to go to get the best value for money that meets their needs. Some third sector and commercial organisations target older people and are more likely to provide appropriate cover taking age and health into consideration. Third age organisations hope that the secondary legislation relating to financial services in the Equality Bill will make it easier for older people to obtain quotations for travel cover and that prices differentials will be proportionate to the actual risk.

The ABI have proposed two interventions which could help improve access to travel insurance for older people and these are:

- Signposting - insurance companies who are unwilling to provide a quote to an individual because of their age must provide details of a "signpost" which would give contact details of insurance companies who would be willing to offer insurance to people of that age and;
- Referrals - insurance companies who are unwilling to provide a quote to an individual because of their age must find a partner who would be willing to offer insurance to people of that age and

[120] ABI (2007) The negative impact on elderly people of not including a tailored insurance exemption in age discrimination legislation

[121] Age Concern (2008), An inclusive approach to financial products, ACE, London

then refer the customer on. Currently six to seven major members of the ABI refer people to BIBA (British Insurance Brokers Association)[122] but it is not known how widely this service is used.

Another intervention as identified by the Institute of Actuaries could be the introduction of refined age bands to determine the level of premium paid. In their response to the Equality Bill, they wrote that actuarial techniques could replace the use of age bands with premium rates calculated individually for each age. The Institute believes that the current use of age bands is driven by the need for distributors to have a product which is easy and cheap to sell rather than by technical pricing considerations.

5.2.7 Motor insurance

According to Age Concern and Help the Aged research older consumers report difficulty in obtaining motor insurance (respondent base, 229)[123] and it is access to insurance rather than cost that is the more significant issue for those surveyed. In contrast, ABI research finds that more than 99% of customers aged 65 or over are able to find motor insurance[124]. A Saga Populus survey supports this finding. It found that only 3% of respondents aged 65 years or over (respondent base, 3307) were refused motor insurance because of age and of these only 7% were unable to find any motor insurance. In contrast, no respondents in the same survey, aged 50-64 years were refused cover because of age. Given the larger respondent base of the Saga Populus survey, it could be considered that their findings are more robust and therefore the difficultly of obtaining motor insurance is not as great as some arguments indicate. April 2009 data from Defaqto also demonstrates that older people should be able to find motor insurance cover. According to their data, there are 16 policies with no upper age limits for motor insurance and 10 policies with an upper age limit of 100 years. An interview with the ABI confirmed that in recent years insurance companies have significantly increased their age limits and the trend is expected to continue. The limited number of policies available to older people indicates that for many (as in travel insurance) the issue is one of accessing these policies. There are a limited number of insurers who will take new older customers which restricts the ability of consumers to shop around for the most competitive premium. In 2007, the ABI reportedthat only 12% of motor insurance companies will cover new customers without any age limit[125].

Studies have shown that older drivers feel that being able to drive increases their quality of life[126]. If they are unable to get motor insurance the risk of social isolation/exclusion is increased, particularly where public transport is not a viable alternative[127]. Consequently the individual is less able to pursue a more active independent lifestyle and depression may occur. Age sector organisations have attempted to quantify the value of the consumer detriment caused for those over 65 who do cannot get motor insurance because. They estimate that it is in the region of£35m to £1,010m per year[128].

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[122] Stakeholder interview, 23 April 2009
[123] Age Concern and Help the Aged (2007,) Insurance and Age, Exploring behaviour, attitudes and discrimination
[124] CRA International(2009) Insurance and Age-based Differentiation, ABI Research Paper No.12
[125] ABI (2007) The negative impact on elderly people of not including a tailored insurance exemption in age discrimination legislation
[126] ESRC (2002) Transport and ageing: extending quality of life via public and private transport
[127] Age Concern and Help the Aged(2007), Insurance and Age, Exploring behaviour, attitudes and discrimination
[128] Government Equalities Office (2009), Equality Bill - Impact Assessment, TSO, London

Research from the AA[129] suggests that older people are sensitive to the effects of their ageing and their general health on their driving competence, and that their perceptions of these effects do significantly alter their driving behaviour. It seems that older drivers become aware of changes in their ability brought about by increasing age and worsening health, and they do respond to this realisation by reducing their involvement in driving.

Both the ABI and Age Concern research has found that older people can face difficulty in getting cover when renting cars. Car rental firms purchase 'block' insurance policies that cover their entire fleet of vehicles and some may choose to control their insurance costs by not accepting business from older drivers. The ABI expect the rental to develop in a similar way to the private motor insurance market with niche firms targeting the older driver as demand increases from this group. Until this occurs, individuals may experience a level of detriment arising from the loss of independence offered from driving a car.

As in travel insurance the ABI have proposed the use of signposting and referrals to improve the access of older people to cover. Other interventions which can assist the industry in assessing the level of risk offered by older people are:

- The DVLA's review of the current licensing process. This could change the way older drivers are tested and the new test could be used as a proxy for driving skills in rating;
- Some local authorities such as Bedford have provided driver seminars that provide advice and support to older motorists, to ensure that they can drive safely and with confidence for as long as possible.

Having access to local resources and facilities such as shops, health services and public transport was important for respondents, particularly for those with limited physical mobility or people without their own transport[130].

5.2.8 Home insurance

Older people tend to pay less for household insurance. This is based on the assumption that they are more likely to spend more time in their homes than people of working age, so the house is less likely to be burgled. However, those in low income households are less likely to have home insurance. Currently the ABI is working with the DWP Financial Inclusion Team and social landlords to raise awareness of the need for contents insurance among those in the social housing market. Landlords are being encouraged to facilitate cover through tenants contents insurance schemes. This would benefit those who would be vulnerable to financial crisis following unexpected events such as burglary or flooding and would potentially seek loans to replace content losses, often from unregulated, non mainstream sources.

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[129] Rabbitt, P., Carmichael, A., Shilling, V., and Sutcliffe, P. (2002) "Age, health and driving" *AA Foundation Report FDN32*

[130] Joseph Rowntree Foundation (2007) Understanding resources in later life: views and experiences of older people

5.2.9 Summary

Protection Markets

There are pockets of consumer detriment in protection markets. The main forms of detriment are lack of access to markets, opportunity costs and increasing social exclusion arising from lack of access, and the inappropriate use of age or age thresholds in some insurance markets. Overall, existing research suggests that the materiality and probability of financial loss is relatively small compared to other markets but that the materiality and probability of emotional loss may be greater.

Age organisations claim that there is between £131 million to £1,180 million of consumer detriment for those over 65 years in motor and travel insurance[131]. The Department of Communities and Local government (DCLG) Impact Assessment on the Equalities Bill estimates that a 0-1% fall in travel and motor insurance premiums for the over 65's would represent savings of up to £16.5 million to older consumers, as well as helping them to maintain their independence and mobility for longer. The insurance industry however, claims that costs will increase if age is not permitted as a discriminator in motor and travel insurance.

[131] Experts' Working Group(2008) Age discrimination in financial services

5.3 Banking

As part of the Government's agenda on financial exclusion, older people have been identified as a vulnerable group who are more likely to lack access to banking services. Consequently there have been a number of financial inclusion initiatives in this sector of the market. The risk of detriment in this market is compounded by the fact that those older people without banking services or with limited access to them are also among the population with the lowest incomes. They are also more likely to be subject to financial abuse[132] and/or financial crime[133], as discussed in section 3. The main forms of financial detriment arise from the increased costs individuals incur through lack of a bank account or access to affordable credit. The stress and anxiety resulting from the difficulties faced in managing finances contribute to emotional detriment.

5.3.1 Bank accounts

During the past decade the way older people deal with money has changed. There has been a move to direct payments of benefits into bank accounts and subsequently the need for a bank account has increased. For many older people this will have been their first experience of the banking and financial services sector. In their recent public policy report, Age Concern and Help the Aged noted that 7% of households with someone aged 85+ have no bank account[134] and it is estimated that around 600,000 people aged 65 and over are without access to banking facilities[135]. A number of older people have expressed a preference for managing in cash[136], and Help the Aged research has found evidence of voluntary self-exclusion from normal banking services and a resistance to/confusion about different payment methods such as cheque books, direct debits and various credit options[137].

There has been some evidence that older people may experience difficulties in opening a bank account as they may not have a driving license or a passport which are the often required forms of identification. Third sector and other agencies working with those experiencing exclusion, found identification documentation a major issue to accessing banking services[138], though a bank account might also be refused if individuals lack a credit history or are deemed to have too low an income. However, it appears there is little evidence that older people without bank accounts have been refused[139].

The main source of consumer detriment for older people without a bank account arises from the increased costs that they will incur in managing their finances. They will not benefit from the savings associated with

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[132] Help the Aged (2008) The Financial Abuse of Older People A review from the literature carried out by the Centre for Policy on Ageing on behalf of Help the Aged

[133] Over 65s most likely to be targeted by share fraudsters, warns FSA http://www.fsa.gov.uk/pages/Library/Communication/PR/2009/055.shtml

[134] Age Concern and Help the Aged (2009) One Voice, Shaping our aging society

[135] Financial Inclusion Taskforce (2008) Third annual report on progress towards the shared goal for banking

[136] Financial Inclusion Taskforce (2006) Access to financial services by those on the margins of banking Final report

[137] Help the Aged (2006) Financial exclusion among older people

[138] Toynbee Hall (2008) Access to Banking in the UK - a snapshot of intermediaries

[139] Toynbee Hall (2008) Access to Banking in the UK - a snapshot of intermediaries, Help the Aged (2006) Financial exclusion among older people

being able to cash a cheque for free and with being able to pay bills by direct debit[140] or the ability to access products and services online at more competitive prices. Though some will consider using direct debits, others have been reluctant as they are wary of automated systems and because they prefer to have personal control over transactions[141]. An indication of the financial cost incurred by unbanked older people can be found in research published by Save the Children in 2007[142]. This found that a 'poverty premium' (the notional amount of additional money that a poor household pays for the same good and services over a year) of £1,000 per annum was paid by poorer families due to financial exclusion. A significant proportion of the extra costs listed in this research were specifically linked to lack of access to a bank.

In addition to financial costs, emotional costs will be incurred as older people will have concerns about their ability to manage finances and about the security of the money they hold, as keeping cash in a jam jar or under the bed leaves individuals vulnerable to theft[143].

In response to the changing banking and money transaction environment a number of initiatives have taken place to facilitate bank account ownership, though it should be noted that these have not been targeted exclusively at older people. These include:

- Basic Bank Accounts (BBA) allow consumers to use essential banking features such as paying cheques for free, getting money at cash machines and paying bills by direct debit or standing order and specific provision within the Banking Code around BBAs They are offered by 17 subscribers to the Banking Code. The Banking Code Standards Board has conducted mystery shopping research on the provision of opening these accounts. Research conducted in March 2008 found that that in the majority of cases (86%) applicants were able to obtain information about basic bank accounts and in only 2% of cases, applicants were unable to obtain any information or literature.
- Post Office Card Accounts (POCA) were introduced in 2003 as an alternative to those who could not or did not want a basic bank account when direct payments of benefits were introduced. It is estimated that approximately 40% of holders are pensioners[144]. POCA works effectively like an electronic benefits book: people may withdraw their benefits from the account, a little at a time if they choose, but no money can be deposited and there are no transactional facilities. However, though POCA provides some security, not having a direct debit facility excludes people from this method of paying bills with the consequence of having to pay more for some services, such as utilities, by having to use alternative payment methods. In November 2008, it was confirmed that the contract for POCA would remain with the Post Office until 2015.
- Specific bank actions to assist people in opening bank accounts and/or who lack confidence to enter bank branches. For example, RBS/NatWest recognised that certain groups, such as the elderly, may experience problems when it comes to providing identify & address verification documentation. As a result they made special arrangements for those groups, such as exploring

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[140] Toynbee Hall (2005) Banking the unbanked - a snapshot

[141] Hill, Katherine, Sutton, Liz and Cox, Lynne (2009) Managing resources in later life Older people's experience of change and continuity. Joseph Rowntree Foundation

[142] Save the Children (2007) The Poverty Premium How poor households pay more for essential goods and services

[143] http://www.chesterchronicle.co.uk/chester-news/local-chester-news/2009/04/16/police-issue-warning-to-residents-after-distraction-burglary-in-oakmere-59067-23402013/

[144] Help the Aged (2006) Help the Aged Briefing – Post Office Card Account

ways of developing **'Trusted Partner'** programmes, which allows a partner intermediary, for example a Housing Association, to carry out the Basic Bank Account application and identification verification process outside of a bank branch;

- The Banking Partnership Group was established in April 2008 and brings together key representatives from banking, Government and the third sector to discuss issues relating to 'access to banking' and to inform Toynbee Hall's banking project. Their document 'Developing Inclusive Banking[145]' offers suggestions to banks on how to recognise and reduce potential barriers for customer account opening and ensure that all customers are able to open an appropriate account. At the time of writing this report, no commentary on the effectiveness, or otherwise, of this group has been found;
- The Financial Inclusion Taskforce has the goal of halving the number of adults in UK households without a bank account. Their third annual report published in December 2008 comments that 50% of the progress towards achieving the shared goal has been achieved (based on FRS data for 2006/07 which shows that up to 2.1m people, living in 1.4m households do not have access to a bank account of any kind). However, though no specific reference is made to older people, it is noted that progress towards the shared goal has slowed or stalled during the past year which is comparable to the earlier Help the Aged/Age Concern comment that the number of households with someone aged 85+ with no bank account has remained unchanged in the last year.

The potential for consumer detriment in banking is not found solely among the unbanked. Help the Aged has expressed concern that the changes in the way we use money is causing confusion and worry for many older people which in turn could facilitate increased financial abuse of older people[146] leading to financial loss. The greater use of internet and telephone banking, PIN numbers, and the withdrawal of cheques as a means of payment means many older people are finding themselves left behind as online banking grows and the numbers of branches at local level declines[147]. The growth of online banking puts older people at a disadvantage as only one in five older people have internet access at home, according to Help the Aged in their 2007 policy statement on financial services. Declining cognitive abilities are also a contributory factor to the difficulties (such as confusion and anxiety) that PIN technology presents to older people.

There are mixed reports about the detriment older people might experience with premium bank accounts, which often include a number of benefits, among them worldwide family multi-trip travel insurance. Help the Aged say they receive many complaints from individuals who have had such accounts and found at the age of 65 or 70 that they are no longer eligible for the insurance-related benefits. Some of these concerns may reduce if other banks follow the lead of Alliance and Leicester who have introduced a premier current account aimed at the over 50s which offers annual worldwide travel insurance up to the age of 79 among its benefits.

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[145] Toynbee Hall (2009) Developing Inclusive Banking

[146] Help the Aged (2008) The Financial Abuse of Older People, a review from the literature

[147] Help the Aged (2007) Financial Capability: the Government's long-term approach and Thorensen Review of Generic Financial Advice A policy response by Help the Aged

It has also been suggested that banking services discriminate based on age. Though banks do not overtly appear to discriminate against older people there is a feeling among older people that credit is often refused based on age. This view has been reinforced following the issue of the new Code of Banking Practice at the end of March 2008.Mike Young's recommendations for the Code had included: "The guidance should be amended to ban credit rejection simply on the grounds of reaching a certain age." The banks did not accept this recommendation on the basis that the decision to grant credit includes an assessment of risk and age is an indicator of risk. In their view, not to consider age could leave a bank open to the accusation of irresponsible lending.

Bank closures have restricted access to banking services for some older people as they no longer have easy access to bank branches. ATMs (Automated Teller Machine) therefore play an increasing role in providing access to cash for older people. APACS data for 2006 shows that over 50% of the UK's cash machines are located at non-bank branch sites. A few years ago concerns were raised about charges for use of ATMs as these were more likely to impact on vulnerable groups, such as the elderly, who had restricted access to these machines. Today, Link report on their website that "over 96% of all ATM cash withdrawals by UK cardholders in the UK are free of charge". ATMs in turn present problems for older people who have to remember a PIN and who may be reluctant to use machines. Where older people are dependent on others to access their cash (for example, poor to limited mobility, poor memory, dementia), the use of cards and PIN can present a problem. If an older person is unable to go to the bank, their only option is to give these to family members, friends or care workers to take out the money for them. If this trust is abused, police are unable to pursue the case because the individual has knowingly given their PIN to someone, which the banks tell you not to do. The British Bankers' Association is aware of the problem and they are working with Help the Aged to find a way forward with this problem.

Since the introduction of 'chip and PIN' cards, APACS have tried to raise awareness of the availability of the alternative 'chip and signature' cards among retailers and consumers. These are of benefit to older people who may have difficulty in remembering a PIN. According to APACS, only a small number of 'chip and signature' cards have been issued. Recent threads on internet money forums indicate that a lack of awareness by retailers on how to process transactions on these cards may contribute to their low take-up[148].

There are a number of interventions in place to reduce the risk of detriment in banking. These include:

- The Financial Services Compensation Scheme will pay compensation of up to £50000 where a deposit taking institution defaults and its customers suffer a financial loss. In most recent times, this has included Icesave, the UK branch of Landsbanki;
- Credit Unions offer older people a local banking alternative to manage their money. However, due to limited access to them, they are not a viable option in some parts of the UK, such as the South East;
- To date rules around how banks sell current and saving accounts or credit products have been self regulated through a voluntary banking code administered by the Banking Code Standards Board.

[148] http://forums.moneysavingexpert.com/showthread.html?=1633149

Following a recent consultation reviewing regulations around banks' 'conduct of business'[149], the FSA announced in April 2009 that it will take over all retail banking conduct regulation for deposit taking and payment services in November 2009[150].

5.3.2 Credit

In this section, credit comprises a wide and diverse range of products and services including: personal loans; credit and store cards; credit linked to the purchase of goods or services (store credit, hire purchase, conditional sale); mortgage lending (not equity release); cheque cashing and pawn-broking. This section relates primarily to unsecured credit as information relating to each of these listed products and older people is not available Mortgages are covered in the section below.

The awareness of the risk of detriment among older people due to debt has risen in recent years with third sector organisations such as Help the Aged, Citizens Advice Bureau and CCCS (Consumer Credit Counselling Service)raising the profile of the issue as well as Prudential's research[151] on pensioners. CCCS says that the over-50s now have the biggest outstanding card debts of any age group.

Traditionally debt has not been considered an issue for older people and for the vast majority of older people, this situation is largely unchanged. Most people do not enter retirement with either unsecured credit commitments or mortgages; and the proportion doing so has not increased dramatically[152] . However, though credit use falls with age, research finds that those who owe money when they retire owe substantially larger amounts than their counterparts of ten years ago[153] and it is felt that there is some evidence of a 'spend it before you go' mentality emerging[154]. Recent findings from Help the Aged's Your Money Matters programme[155] reinforces these views and identifies that younger older people were more likely to seek help with problems related to debt, and were more likely than those at the older end (up to 100 years) to have multiple debts.

From FSA analysis on the lack of financial capability of older people in categories C2, D and E, a picture emerges of the more vulnerable categories of older people turning to various forms of credit, but without the financial history to gain access to more attractive credit facilities. Difficulties in securing mainstream credit can lead them to gravitate towards unregulated sources of credit associated with poor value products and high charges. A CAB (Citizens Advice Bureau) Scotland survey finds that there is a trend for clients to hold more sub-prime debt as they retire and advance in years. This is likely to represent the difficulties in securing mainstream credit as clients get older and have lower incomes, but it also shows that clients continue to need credit as part of their income into their 70's and retirement years[156].

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[149] FSA (2008) CP08/19: Regulating retail banking conduct of business

[150] FSA (2009) PS09/6 Regulatory retail banking conduct of business – Feedback on CP08/19 and final rules

[151] Prudential Lifetime Mortgage research shows pensioners are facing retirement debt, 20 July 2006, http://www.moneynews.co.uk/2192/prudential-lifetime-mortgage-research-shows-pensioners-are-facing-retirement-debt/

[152] Help the Aged (2008) Debt and older people How age affects attitudes to borrowing

[153] Help the Aged (2008) Debt and older people How age affects attitudes to borrowing

[154] http://news.bbc.co.uk/1/hi/programmes/moneybox/default.stm

[155] Help the Aged (2009) Your Money Matters evaluation Money management for older people

[156] Citizens Advice Scotland (2008) Growing old together: Older CAB clients and debt

Anecdotal evidence[157] suggests that debt problems among older people are on the rise and this will only continue to grow as the current economic downturn continues with the resulting financial consequences of high interest charges and in worse case scenarios, the societal burden incurred due to IVAs (Individual Voluntary Arrangements) or bankruptcy as well as the associated impact on a person's mental wellbeing, that is, stress, depression and a sense of insecurity[158]. Bankruptcy statistics for 2007 show that those aged over 65 years of age represented 7% of bankrupts in England and Wales (over 4,000 people)[159]. Since 6 April 2009, a Debt Relief Order (DRO), a form of insolvency that lasts for 12 months, is available to help people who have relatively low debt, little surplus income and few valuable assets and who have no realistic chance of paying off their debts within a reasonable time.

A number of interventions exist to prevent credit issues or assist those in need of help. A number of these are in relation to the government's financial inclusion agenda. Interventions include:

- The Social Fund which was introduced in 1988 with the aim of providing a variety of forms of financial support to people on low incomes. The scheme is available to people of all ages. For older people, the Social Fund can be regarded as a potential supplement to other state benefits. However, it has not been considered a success in providing financial support to older people. Take-up has been low among older people with only one in 200 older people having a Social Fund Loan[160]. A lack of knowledge of the scheme has been identified as the major barrier[161] to take-up;
- The Growth Fund which makes accessible credit available to people outside the mainstream lenders through credit unions and community development financial institutions (CDFIs);
- Regulation which includes the Consumer Credit Act 2006 which requires lenders to lend responsibly and the FLA (Finance and Leasing Association) lending code;
- Debt counselling services such as National Debtline, Consumer Credit Counselling Service, and CAB with other related assistance from organisations such as Help the Aged/Age Concern.

5.3.3 Mortgages

For at least the past decade, people have needed to borrow more and for longer in order to purchase property. This, coupled for some, with the failure of endowment mortgages to meet the total repayment balance has led organisations such as Help the Aged to comment "there is concern that people may be entering into retirement with outstanding mortgages and credit commitments that cause them to get into financial difficulty"[162]. In this situation, the ability to manage finances can be a key issue for older people as they manage a reduced income but with potentially significant monthly outgoings. Recent research from

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[157] Various media stories and press releases

[158] Balmer, N. (2006) 'Worried sick: the experience of debt problems and their relationship with health, illness and disability', Social Policy and Society, Vol. 5, No. 1,
pp. 39–51. Pleasence, P., et al (2007) A Helping Hand: The Impact of Debt Advice on People's Lives. LSRC Research Paper No. 15. London: Legal Services Commission

[159] http://www.becomingbankrupt.co.uk/bankruptcy-statistics.html

[160] Price, Dr. D (2008) Financial issues facing older people, meeting of the Oddfellows

[161] DWP (2002)Social Fund use amongst older people

[162] Help the Aged (2008) Debt and older people How age affects attitudes to borrowing

Key Retirement Solutions[163] finds that an increasing number of pensioners who approach them have mortgages which continue well into retirement and they estimate that the average mortgage debt for those aged 65 and over is £43,069. It is also estimated that about one in 20 older people have mortgages into their 80s[164].

In 2006 concerns were expressed about the volume of interest only mortgages being sold to older people,as a number of lenders do not have an upper age limit. CML (Council of Mortgage Lenders) data provided to The Times in 2006 [165] showed that more that 18,000 pensioners had taken out home loans or remortgaged on the previous 18 months. Consumer groups, including Citizens Advice and National Debtline, say they have been approached by retired people who have been sold mortgages that they could not afford to repay. The FSA conducted an investigation into mortgages in retirement to determine if banks and building societies were lending responsibly. Their subsequent report Guidance on Mortgages Running into Retirement[166] aims to help mortgage lenders to comply with their responsible lending rules.

Regulatory interventions are in place to prevent older people reaching retirement with significant outstanding mortgages. The

- FSA's MCOB (Mortgage Conduct of Business) rules, such as MCOB 11.3.1R requires providers to make affordability assessments for each customer, before entering into a regulated mortgage contract with them and the FSA's 'Principles for Business', Principle 6 requires that "a firm must pay due regard to the interests of its customers and treat them fairly". A mortgage lender cannot limit assessment of affordability in retirement to certain categories (e.g. those over a certain age or those with mortgages stretched more than a certain number of years beyond retirement). They must assess the position of all customers who could reasonably be anticipated to face changed circumstances upon retirement. However in the FSA's Financial Risk Outlook 2009, the effectiveness of this rules appear to be questioned when the following statement was made "Too many firms failed to adequately establish consumers' needs, with senior management failing to ensure that customers were treated fairly".

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[163] UK Pensioners turn to equity release to repay growing mortgage debt, 20th April 2009 http://www.keyrs.co.uk/about-key/press-office/news/uk-pensioners-turn-to-equity-release-to-repay-growing-mortgage-debt

[164] Price, Dr. D (2008) Financial issues facing older people, meeting of the Oddfellows

[165] Pensioners join the mortgage generation, The Times, 5 December 2006, http://property.timesonline.co.uk/tol/life_and_style/property/article659920.ece

[166] FSA (2007) Mortgages running into retirement Examples of good and poor practice for mortgage lenders

5.3.4 Summary

Banking and credit

In recent years, the financial inclusion initiatives in banking and credit have reduced the risk of detriment among low income older people, while tighter regulation and increased compensation levels have reduced the potential for financial loss. Nevertheless some older people still do not have a bank account (some by choice) and will suffer detriment arising from the 'poverty premium' incurred. The increasing use of technology in banking services, through 'chip and PIN' and internet banking will increasingly isolate those who lack confidence in accessing cash and making and receiving payments electronically or who do not have access to the internet. Regulatory interventions requiring lending organisations to assess an individual's ability to pay significantly reduce the potential for detriment among older consumers in this market. Though debt (either unsecured or relating to a mortgage) is not an issue for the majority of older people, where it does occur, its impact is likely to be more significant on those affected as those who owe money when they retire owe substantially larger amounts than their counterparts of ten years ago.

5.4 Savings & Investment

As noted above, a significant proportion of those in later life have savings and investments other than their pension fund. For many, savings take the form of cash held in bank or building society savings accounts (including cash ISAs, premium bonds or national savings). A smaller proportion also has investments such as equity ISAs, investment bonds or unit trusts). Some of the later life group may also have endowment policies which may or may not be designed to pay off their mortgages. All will have experienced falls in either the value of their capital and/or the income derived from it as a result of recent falls in the stock market and interest rates.

5.4.1 Savings accounts

Those saving in cash-based accounts are exposed to two main forms of risk: the risk of changes to interest rates and counterparty risk (the risk that their savings institution could collapse). In addition, savers in later life may suffer detriment by failing to maximise their interest by shopping around and regularly reviewing their accounts.

Interest rate volatility

The subject of cash savings among the retired has been the subject of many media headlines in recent months (late 2008 / early 2009) due to the unprecedented decline in UK base rates and the reflection of this in interest rates offered by savings institutions. Many older people come to rely on interest from savings accounts to supplement their income in retirement. Many will find themselves not being able to claim pension credit due to the value of their assets but no longer be in receipt of any income from those assets (although the 2009 budget did increase the amount that individuals can hold and still claim pension credit). Some will find themselves having to dip into their capital to maintain living standards, thereby reducing any future income from their savings.

That many of those in later life have significant exposure to interest rate risk has never been as obvious as in today's market. Whilst it is likely that most will have understood that their interest could rise and fall, it is less clear whether any would have anticipated levels of interest close to zero. Whilst disclosure rules require equity investments to disclose the risks and effect of rises and falls in equities values and income levels, it is perhaps questionable whether the equivalent risks in cash based products are highlighted in the same way. Certainly, the FSA's suitability requirements are not applied to those organisations selling or recommending a savings account.

Shopping around

Newspaper headlines have also highlighted institutions failure to reward loyalty among savers. In May 2009, the Financial Times[167] highlighted the poor rewards for loyalty with new accounts at some banks being offered interest rates in the region of 3% whilst existing accounts attract only 0.1%. Whilst not a new

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[167] Financial Times (8th May 2009), Savers told to switch from rock-bottom ISAs. http://www.ft.com/cms/s/2/7bd5fa50-3bf7-11de-acbc-00144feabdc0.html accessed 12th May 2009

issue, the disparity once again highlights the need for those with savings to shop around and move their money. For some of those in later life, the ability to compare deals may be difficult, because of lack of access to information sources (the internet in particular), a lack of confidence in their own ability to compare and make a decision or reduced cognitive abilities. Either way, many of those in later life who perhaps should be moving their money to attract higher rates are unlikely to be doing so.

Counterparty risk

For some, this uncertainty over interest rates has been compounded by the fear of collapse of their savings institution. During 2008 (starting with Northern Rock) and the early part of 2009, several UK banks have come close to collapse and have either been rescued by the private sector or by the Government. Several overseas banks (particularly Icelandic banks offering high interest rate accounts in the UK) have needed to be rescued and for some, national and international compensation schemes have come into play. The situation has highlighted the different compensation measures applied to overseas banks operating in the UK market. For UK-based banks, the rules on compensation have been changed to reflect the public's concern and recent calls on the scheme. Whilst there are exceptions and the details can be complex, compensation levels for customers of most UK-based banks or building societies has been extended to £50,000 per institution. Customers of banks in other EU countries may be subject to different compensation schemes and levels of protection. Consumer awareness of compensation schemes has been heightened by recent events and many consumers are thought to have modified their behaviour by spreading their funds across several institutions, thus reducing their risk exposure. We did not find any data on how many consumers continue to hold in excess of £50,000 with any individual organisation. Recent headlines have criticised the West Bromwich building society for launching a bond in which customers were required to invest more than the compensation limit of £50,000 to achieve a high return.

Details of claims on the compensation fund in 2008/09 were not available at the time of writing but some building societies publishing results were attributing a fall in profits to the levy they have had to pay to the FSCS. Several societies have posted significant falls in profits with some posting losses. Recent reports have suggested that a number of building societies are under pressure with many being downgraded by rating agencies. At the time of writing some financial journalists were sceptical of the ability of some societies to remain independent and the FSA is reported to have launched a crackdown on societies who have ventured away from their traditionally conservative business models. The most recent to face difficulties was the Dunfermline Building Society. Merger is the usual solution for such societies; in the case of Dunfermline the Nationwide acquired many of its assets and liabilities. We are not aware of any major financial detriment suffered by customers of UK building societies and the Government has stepped in to protect the savings of those in UK banks. Some customers have however lost money through savings with Icelandic banks and other overseas banks that have collapsed. Most have been afforded some protection by compensation schemes up to the limits of those schemes.

5.4.2 Endowments

Whilst sales of mortgage and other endowments has fallen in recent years, many older consumers may still have policies taken out when younger. Some currently approaching retirement today will be planning to use their endowment to fully or partially repay their mortgage. During the last few years of the 20th century and the first few years of the 21st, the FSA undertook several reviews of the mortgage endowment market and imposed on firms the additional requirements to inform consumers of potential shortfalls, their options for restructuring their policies or other mechanisms for repaying their mortgage and to alert them

to their rights to complain. Compensation arrangements were put in place and many consumers received compensation from providers on an individual basis where misselling could be demonstrated. The FSA continued to monitor progress in detail until 2005 when research suggested that most consumers with endowment mortgages had either acted to restructure their finances, had complained or intended to complain[168]. Since then, the issue has not gone away , with 7,410 new claims submitted to the FSCS relating to mortgage endowments in 2007/08 with average compensation of £1,800 paid out during the year. In the same year, FOS saw 13,778 new complaints, down from a peak of 69,737 cases in 2005. Most cases continue to be complaints about the sales process and advice received.

5.4.3 Investment Bonds

For many years, investment bonds have been a major source of revenue for the life assurance industry and financial advisers. They have offered customers some tax advantages over unit trust investment and have provided access to with profits funds, although many of the tax advantages were removed by recent changes in capital gains tax.

The main risks that buyers of investment bonds face are: high charges when compared to some alternative investments; an unexpected erosion of capital when taking an income; unexpected loss of capital arising from investment risk that has either not been explained clearly or not understood that can lead in turn to a fall in income; capital loss due to the collapse of an insurer; opportunity cost arising from investment in bonds when ISA allowances have not been used in full. In his report to HM Treasury in 2002, Ron Sandler suggested that detriment might arise, particularly in the with profit bond market due to commission bias, complexity and high charges[169]. Since that time, sales of investment bonds and with profits in particular have fallen away but continue to be significant for some life offices.

Research for Age Concern in 2008 showed that 80% of investment bond holders were aged over 50 and 24% were aged over 75[170]. If there is any consumer detriment suffered in this market, the vast majority will fall on those in later life.

The web-site 'Find.co.uk' suggests that investment bonds may be recommended in a number of situations[171]:

- If you are a higher rate taxpayer seeking an extra income, an investment bond may be recommended because you make 5 per cent annual withdrawals, for twenty years, without any immediate tax liability;
- If you are retired and want a supplementary income, but you are in danger of falling into the age allowance 'trap.' This is the situation whereby the extra personal tax allowance you receive when you are 65-74 (£9,180 for 2008-09 is reduced if your annual income exceeds a certain level (£21,800 for 2008-09). Annual 5 per cent withdrawals from investment bonds do not count towards

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[168] FSA (2005), Mortgage endowments: Progress report and next steps
[169] HM Treasury (2002), Sandler Review: Medium and Long-Term Retail Savings in the UK
[170] Age Concern England (2008), Beyond Financial Inclusion, analysis of the FSA's Baseline Survey of Financial Capability (2006).
[171] Find.co.uk (2009), Investment Bonds Guide, http://www.find.co.uk/investments/funds&trusts/investment_bonds_guide, accessed 12th May 2009

your income, so it will not affect your age allowance. However, before you cash in your bond, you will need to consider how your age allowance might be affected in that year.

- If you are an active investor with a large investment portfolio and you have already mopped up your annual capital gains tax allowance (£9,600 in 2008-09), using an investment bond to manage your investments means you will not be liable for capital gains tax when you make switches between funds;
- If you are trying to shelter capital from inheritance tax through a discounted gift trust or loan trust, life insurance companies often sell packaged products whereby these trusts are linked to investment bonds. The advantage of using an investment bond is that the investment income in trusts will generally be taxed at 40 per cent, but when it is accumulated within a bond it is only taxed at 20 per cent;
- If you are an investor who is likely to need long term care, life insurance policies are not normally be counted as part of your means when your eligibility for local authority funding is assessed.

The website also suggests that charges on investment bonds may be higher than equivalent unit trust products, that higher commission rates are available on such products and that some higher rate taxpayers may find themselves paying higher tax on investment bond income than they would on capital gains on unit trust transactions.

Little empirical data has been found to fully quantify the extent to which those who are sold investment bonds suffer from detriment, although plenty of anecdotal comments (from the media and organisations such as Which?) suggest that investment bonds with medium to high risk exposure continue to be sold to consumers with a low risk appetite. Which? and the national press have often highlighted the banks as the main culprits for misselling of bonds, for example:

"Financial adviser battles HBOS over bad advice" Citywire, March 2009[172]

Data from the Financial Ombudsman Service (FOS) suggests that just 1% of its complaints concern investment bonds and that the number of new complaints per year has fallen from 2,601 in 2007 to 1,192 in 2008, although investment bonds continue to attract more complaints than any other form of packaged investment product. Complaints tend to take the form of concerns about Market Value Reductions (MVRs) which can be applied to withdrawals from with profit funds; poor fund performance; and the way in which inherited estates of with profits companies are being handled. Many of these complaints do not fall within FOS' area of responsibility and are passed back to the FSA to be dealt with. The Financial Services Compensation Scheme (FSCS) would come in to play in the event of either a life assurer managing investment bonds being in default or a financial adviser in default with claims of misselling investment bonds. The former has not occurred in the UK for many years.

Recent moves by one life company to increase the trail commission on their investment bonds could lead to increased sales of these products, particularly if the move is followed by others. If the increase in commissions (and perhaps charges) does affect future sales, some consumers could find themselves advised to invest in these products when others may offer better value. Whilst the suitability rules should

[172] http://www.citywire.co.uk/Personal/-/news/markets-companies-and-funds/content.aspx?ID=333168

reduce the scope for this to happen, in 2002, the FSA reported that investment bonds can be subject to commission bias[173] which suggests that some scope for detriment might arise.

5.4.4 Unit trusts and OEICs / Investment ISAs

There are few examples of misselling of traditional unit trusts or investment ISAs but the sector is not totally immune from criticism. In recent years, several thousand cases of misselling of split capital have been referred to the FSCS and FOS, with some resulting in compensation. More recently, Barclays has hit the headlines with claims made of misselling of a high risk fund to risk-averse (mainly older) investors. Both cases highlight the potential for consumers to fail to recognise the risks to which their investment decisions expose them and the scope for advisors to mis-sell remains.

5.4.5 Structured products

The collapse of Lehman Brothers in 2008 and the effect of the current economic climate have highlighted the risks that consumers can take investing in structured products. Many corporate and individual customers of Lehman lost money in the collapse of the firm and compensation through the FSCS has not been available. The press has reported on a number of supposedly sophisticated investors who claim not to have understood the risks to which they were exposed[174].

The expression 'structured products' includes a wide range of product types with the common link being the use of derivatives to provide different forms of guarantee, usually of the principal invested with returns often linked to an index or other benchmark. Some products fall under the banner and protection of packaged products, others are not, are not afforded the same protection but have more restrictions in who they can be sold to. Many lack transparency in terms of costs and risks to which they expose customers. One earlier example of problems with structured product arose in 2004, when the FSA became involved in a review of Precipice Bonds, with the FSCS paying out several million pounds in compensation for poor advice and other firms compensating their customers. Whilst these bonds are no longer available and disclosure requirements have been tightened as a result, several financial organisations promote products with guarantees that kick in at different points: some at maturity, some throughout the contract. Others are promoting income guarantees. The cost of these guarantees is the subject of considerable debate with some commentators suggesting that the cost may be so high that investors can get no return on their investment, simply the guarantee of the return of capital[175].

In uncertain economic conditions, the question of provider resilience also raises concern when guarantees are being offered.

[173] FSA, CP121, "Reforming polarisation: making the market work for consumers", January 2002.
[174] ????
[175] Money Marketing, April 2009. Market Conditions ask new questions of structured product providers.

5.4.6 Summary

Saving & Investment

Recent turmoil in markets and economies has highlighted the lack of resilience that both consumers and financial institutions have to extremely difficult conditions. Whereas concerns in the past have been focused on equity-based products, much of the concern in the past year and many of the complaints against the industry have been focused on the banking and building society sector. The risk of major banking insolvency allied to a collapse in interest rates has made the previously 'safe' haven of cash much less comfortable. Many older consumers have experience finance loss, a much-reduced income and often considerable stress worrying about the security of their money. One bright light that emerges from the gloom is that consumers, particularly those relying on savings are generally more aware of the risks they take and the remedial services that protect them.

Equity-based investment products continue to raise concerns, with the perennial uncertainty about the value for money of investment bonds and the costs and risks of structured products.

5.5 *Information, Guidance & Advice*

We have referred in previous sections of this paper to the widespread asymmetry of information prevalent in markets, a factor which was highlighted by Ron Sandler in his review of savings and investment markets for HM Treasury in 2002. He suggested that consumers were in a particularly weak position in financial services markets, a position which led to high levels of sales regulation and resulted in advice not being widely available. Since then the provision of information, guidance and advice has been at the heart of the Government's National Financial Capability Strategy and several attempts have been made to restructure the advice, sales and distribution sectors; the latest in the form of the FSA's Retail Distribution Review.

Consumers have been shown to make poor financial decisions, including the decision to do nothing. This leads to detriment in the form of poor product choices which in turn can lead to a loss of capital or income. The decision to do nothing can lead to consumers missing opportunities that could improve their financial position in both the short and long term. Behind these poor financial decisions sit a number of factors: inertia caused by lack of awareness of options or a lack of trust in financial institutions and their products; poor levels of financial literacy; poor levels of financial capability, particularly planning ahead; and limited access to appropriate information and advice.

One feature of today's later life cohorts that marks them out from younger generations is the very different approach to technology. Over time this is expected to change as new cohorts enter later life. The emergence of the silver surfer is evident with nearly 1/3rd of those aged 65 or over using the internet (Figure 8 below); Google 'internet sites for the over 50s' and many social networking and information sites are revealed; many of which contain financial information relevant to later life. However, it remains the case that the majority of the over 65s never use the internet. As more and more day-to-day financial matters are transferred to new technologies, many older consumers are at risk of being excluded from markets, and inertia is reinforced.

Help the Aged also point to the increased difficulties in getting access to information and advice for those who have restricted social networks (due to lack of mobility or limited family and friends):

"Lots of things happen today which I don't know about or understand and I feel cut off" quote from Help the Aged report[176]

The report also states that many older people do not like to bother others for financial help or advice but that 96% felt that more could be done to help older people with money matters, particularly new technologies in financial services. DWP has also conducted research into the service needs of vulnerable pensioners and confirm that many feel lonely and isolated and struggle to cope with changes in society, including changes to financial matters[177].

We consider below ways in which a lack of access to information, guidance and financial advice is being addressed.

Figure 8: Use of internet by age[178]

[176] Help the Aged (2007), Lost in the Money Maze

[177] DWP (2005), Understanding the service needs of vulnerable pensioners: Disability, Ill-health and access to the Pensions Service

[178] ONS (2008), Internet Access 2008 Households and Individuals

When adults last used the Internet, by sex and age groups, UK, 2006, 2007 & 2008

	Within the last 3 months			More than 3 months			Never used it		
	2006	2007	2008	2006	2007	2008	2006	2007	2008
Per cent									
Men	65	71	75	5	5	4	30	23	20
Women	55	62	66	5	6	5	40	31	29
All	60	67	71	5	6	5	35	27	25
Age groups									
16-24	83	90	93	7	6	..	10	4	..
25-44	79	80	87	5	6	5	17	13	8
45-54	68	75	78	6	6	..	26	19	17
55-64	52	59	63	5	5	..	43	35	33
65 plus	15	24	26	3	5	5	82	71	70

5.5.1 Information and guidance

We have noted several instances where a lack of information, or the ability to assimilate information, can lead to detriment in later life, including:

- In the decumulation market, concerns about awareness of the OMO and annuity choices;
- In the protection market, a lack of information about the availability of insurance in older age;
- In the savings & investment market, a lack of awareness over risks posed by different products;

Moreover, analysis of the FSA's Baseline Survey of Financial Capability shows that scores in the domain 'Choosing Products' fall in later life, even taking account of lower levels of purchasing activity. Analysis conducted for Age Concern in 2008 also showed a lesser tendency among older groups to shop around at insurance renewal. A recent evaluation by Citizens Advice Bureau (CAB) also highlighted the significant gap in the provision of financial advice to older groups[179].

Several initiatives have been designed to fill the gaps in information, some generic and others specific to those in later life. We summarise below just some of those initiatives. Other initiatives not covered in detail include the money advice work carried out by Citizens' Advice, the work of the Pensions Advisory Service, and a wide range of other third sector organisations.

Financial Capabilitiy

The FSA's Financial Capability strategy has, to date, focused on younger groups with low levels of financial capability. Information has been supplied predominantly through the FSA's MoneyMadeClear (MMC) website, brochures available from the website and other local sources, and a programme of partnership

[179] CAB (2009), Money Plan (evaluation of the pilot)

initiatives. Many of the topics covered by MMC have also been relevant to older groups; for example information on pensions, savings and investments, credit etc. However, the FSA has recently carried out a review of its strategy for older people and has announced in its plans for 2009/10 its intention to explore whether more tailored MMC information can be delivered to those in later life[180]. The FSA has identified three areas of need where information gaps exist in later life: Nearing Retirement; financial decisions relating to ill-health or the need for care; and financial decisions relating to bereavement and divorce or separation.

Money Guidance

The Money Guidance Pathfinder which is being managed by the FSA and HM Treasury under the MMC brand, is designed to help address the gap between straightforward information and regulated financial advice. The service is open to all but focused to some degree on 'those most vulnerable to the consequences of poor financial decision making'. The partners selected by the FSA and HMT include Age Concern England who are delivering guidance in the North of England. It is not known at this point in time how successful the wider service will be at reaching those in later life. It is expected that the Panel will start to receive feedback on the results of the Pathfinder as the year progresses.

Your Money Matters

The Your Money Matters (YMM) programme was a free, confidential and impartial money advice service for older people run by Help the Aged in partnership with Barclays. The programme was launched in 2006 with three years of funding from Barclays which ended in April 2009. The aims of the YMM programme were to:

- Improve people's knowledge, skills and confidence to manage their money;
- Provide practical assistance to overcome money management and debt problems;
- Raise awareness of the issues of older people, debt and money management.

The project provided help to over 2,500 older people through one to one cases and held over 400 group awareness sessions to more than 7,000 people. The project found that widows were a distinct group of older people lacking in financial capability.

The evaluation of the service found that:

- Over three-quarters of interviewees reported that their financial situation had improved as a result of contacting Your Money Matters;
- Almost half the older people interviewed thought that participation in Your Money Matters had a positive impact on their knowledge and their confidence in managing money.

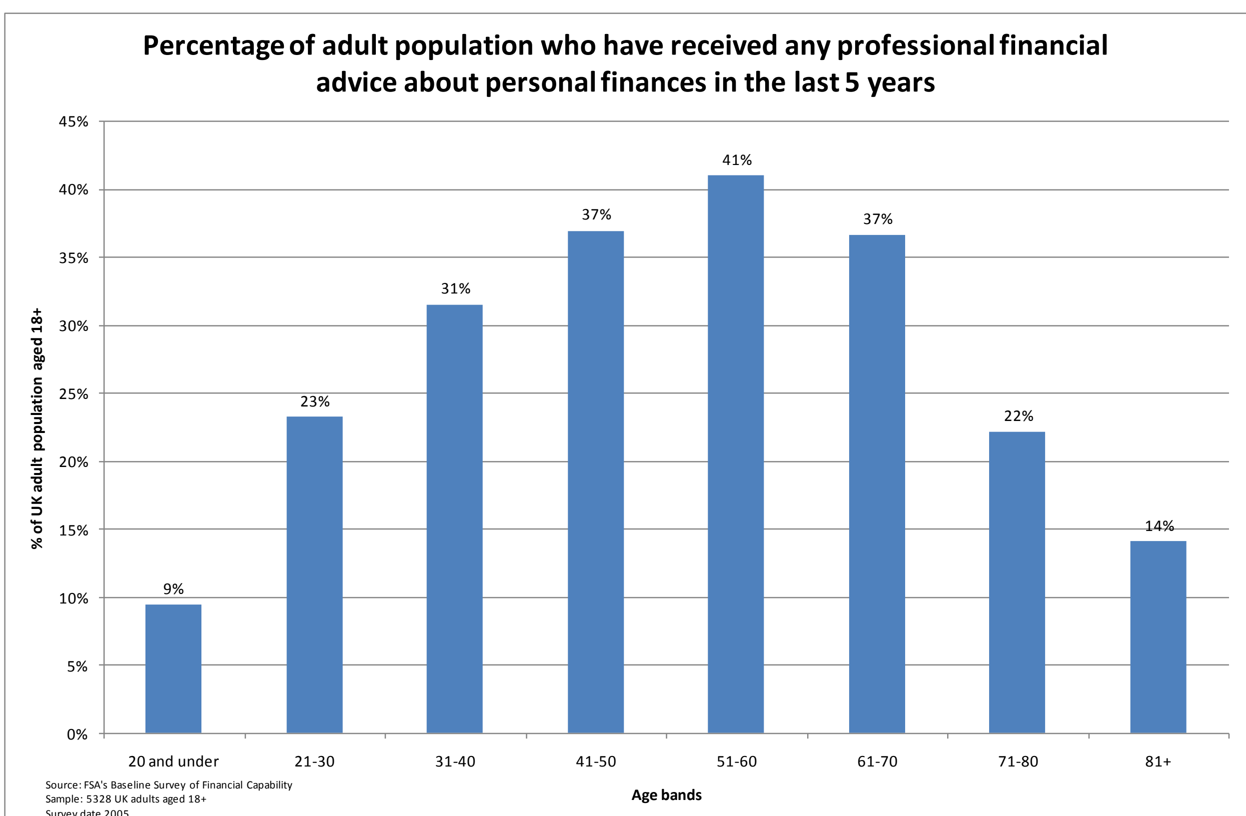
It is not clear whether the service will continue. However the main improvement to Your Money Matters suggested by partner organisations, by advisers and by clients, all related to capacity – more projects and more advisers were called for to meet the perceived need for this type of money advice service.

[180] FSA (2009), Business Plan 2009/10

5.5.2 Regulated Advice

Whilst many people in later life may have taken financial advice at some point in their lives, few will have an on-going relationship with a financial adviser. As Figure 9 below shows, use of a financial adviser tails off with age. However, several people interviewed for this project remarked that this is due more to inertia or lack of trust than it is to the lack of need for regular reviews. It may also be a consequence of a large proportion of the older population failing to meet the income or wealth minima set by many commercial advice organisations.

Figure 9: Percentage of adult population in receipt of financial advice by age



Although the number of intermediary firms specifically targeting the older population is on the increase, it remains the case that many older people do not seek out or receive financial planning advice. Some, but not all, may suffer detriment in terms of missed opportunities whilst others may make inappropriate product choices without advice.

The FSA has for many years been seeking ways of encouraging the industry to fill the advice gap[181] that many claim is a source of social and financial exclusion. Earlier attempts to develop basic advice followed the Sandler Review but largely failed. The FSA is now part-way through the planning and implementation of the Retail Distribution Review. The feedback paper published in November 2008[182] sets (among other things) out the desire to create a clearer and simpler landscape for both advice and 'guided sales', and in doing so to encourage more firms to develop guided sales channels. Whilst guided sales may not be

[181] ABI (2002), Closing the Savings Gap: Why the savings industry wants change

[182] FSA (2008), Retail Distribution Review Including feedback on DP07/1 and the Interim Report

suitable for all of the needs of those in later life, it may help in some situations, such as choice of annuity (indeed the PADA proposals look a little like guided sales). A further consultation paper is anticipated in June 2009 but it is the industry response to that which will determine whether extra capacity for advice and non-advised sales is injected into the market or whether the new proposals for independent advice cause a further contraction in the market.

Another recent development with relevance to those in later life is the 'Later Life Adviser Accreditation' developed by the Financial Services Skills Council (FSSC) and launched in 2008. The aim of the scheme is to create a pool of advisers with a high level of competence able to advice the older market. It is not clear how many advisers have yet achieved accreditation nor what the future of the scheme is in the light of the Government's recent decision not to re-licence the FSSC.

5.5.3 Summary

Whilst younger people are possibly better served for information regarding financial than they have ever been, albeit that there is scope for information overload, older generations are often excluded from the growth in consumer-oriented information by:

- their inability or preference to access new technology;
- for some, their lack of mobility or social isolation;
- for some, a lack of trust in financial institutions;
- for others, their preference not to ask for help.

Whilst initiatives are underway to help fill the information and advice gaps for older people, it will be some time before we know whether they have been successful.

6 Market interventions – gap analysis

Sections below summarise where we believe there to be cause for concern, either because the potential for detriment is material, or the probability of detriment is significant evidence of detriment or where there is limited potential for detriment but very large numbers of people are affected.

For each market sector, identify the type of detriment that applies (using framework for detriment) and then assess whether detriment is likely to be material, how probable and relative scale of the issue should it arise (size of market)

- Materiality of detriment = a theoretical measure of the significance or impact of detriment to the individual should it occur, irrespective of current evidence or the probability of it occurring. Not a precise measure. If severe loss of capital / income then red. If high charges / remedy likely to be expensive then orange, if small loss likely to be incurred
- Probability of detriment = a judgement taken about the risk of this type detriment arising based upon degree of existing market efficiency intervention, observations about how effective interventions are.
- Scale of detriment = based on the relative size of a market and indicates how widespread the impact could be if detriment arose

The colour coding used in the following charts indicates:

- Green = materially insignificant / low probability / small market (<0.5 million individuals)
- Orange = materially moderate / medium probability / mid-sized market (0.5-5 million individuals)
- Red = materially very significant for the consumer / high probability / large market (5m+ individuals)
- No colour = not applicable or no evidence of detriment

Decumulation

6.1.1 Traditional Annuities

The main area where detriment is both materially important and has a moderately high probability of occurring lies with consumers' sub-optimal choices of annuity type and uncertainty about whether those choices are informed ones, albeit that improvements in longevity and the risk to the insurance sector should continue to be an area of significant focus. The consequences of single life annuities can be severe for remaining partners if they have little other support and current evidence suggests that there is a moderate to high probability of this risk arising. Whilst improvements in the flow of information to consumers may in time improve the situation, it is possible that further moves could be made to reduce the risk to individuals and society through the supply of information and advice or through a more radical change to the type of annuity that individuals are required to purchase.

Figure 10: Analysis of detriment in traditional annuity market

Traditional Annuities – nature of risk	Materiality of detriment	Probability of detriment
Counterparty risk	**Insurer insolvency could leave consumers without income or reduced income**	**Risk reduced by prudential regulations, in particular ICA and Solvency II, and high level of compensation available from FSCS**
Reduced income from poor choice of annuity	**May suffer some loss of income due to asymmetry of information or delay in payment.**	**Reduced by market developments (enhanced annuities), improved OMO process, sales / advice regulations.**
High charges / costs	**Possible fall in money's worth over time**	**Market shown to be efficient**
Remedial costs	**Process likely to be straightforward**	**FOS, FSCS procedures well-established**
Opportunity costs	**Potential loss of amenity from capital / scope for income growth**	**Improving mortality / volatile markets reduce likelihood.**
Societal burden	**Single Life Annuities (partners left with little income on first death)**	**Current market experience suggests probability moderate (possibly high)**
Emotional / psychological	**Some concern over loss of control over capital**	**Offset by certainty of income**
Scale	**Several million contracts per year and market growing with shift to DC pension accumulation.**	

6.1.2 New-style decumulation products

New style annuities present more uncertainty and potential for detriment. Consumers have the potential to suffer very considerable detriment if they purchase a product which carries risks that they do not understand and markets move against them. Whilst disclosure and suitability rules do constrain the scale of detriment there are growing concerns about this market. Consumers who purchase these products also give up the certainty of an annuity before age 75 and risk losing out as longevity improves and annuity rates move downwards. Emotional stress is also a concern in current market conditions. The market remains small and so the impact is unlikely to be widespread. However, there is potential for the market to grow further as more and more consumers seek to defer annuity purchase for all or some of their pension funds. Additional disclosures, guidance on the suitability of these products, enhanced training and competence requirements for advisers of these products may contain the probability of detriment if the market does grow. Close prudential supervision for companies offering guarantees is require in order to ensure that they are pricing and reserving accurately for the risks involved.

Figure 11 Analysis of detriment in alternatives to traditional annuities

New style products	Materiality of detriment	Probability of detriment
Counterparty risk = loss of income	**Insurer insolvency could leave consumers with no or reduced income**	**Reduced by prudential regulation and FSCS but some uncertainty over risks to providers**
Reduced income from poor choice of annuity	**Loss of capital / income could be high due to risks inherent in some products**	**Reduced by sales regulation but concerns about misselling beginning to increase**
High charges / costs	**High charges can significantly reduce benefits of guarantees and/or flexibility.**	**Some uncertainty about levels and impact of charges.**
Remedial costs	**More complex products – lack of suitability may be harder to prove**	**FOS, FSCS procedures well-established**
Opportunity costs	**Loss of income in longer term due to decision not to buy an annuity**	**Changes in mortality and stock market make this possible.**
Societal burden	**If incomes fall during retirement, more may need state support**	**Current buyers tend to be more affluent and likely to have other income to support them.**
Emotional / psychological	**Concern about impact of economic and stock market conditions**	**Moderate to high in current conditions.**
Scale	**A small but growing market.**	

6.1.3 DB Pensions in Payment

Only one major type of detriment is possible in this sector – members of schemes lose their future income as a result of employer and scheme failure. In recent years, the probability of detriment has been reduced by a tightening of legislation, regulation and ultimate redress. The difficulties brought about by the current environment are recognised by both TPR and PPF and we believe that the probability of detriment remains low but recognise the concerns about the long term sustainability of the PPF and uncertainty about what recourse will be open to members should it become insolvent.

Figure 12: Analysis of detriment in DB pensions in payment

DB Pensions in Payment	Materiality of detriment	Probability of detriment
Counterparty risk = loss of income	**Due to collapse of employer and scheme**	**Reduced by tighter regulation of schemes and PPF.**
Emotional / psychological	**For those in vulnerable schemes, concerns will run high.**	**Low for the time being.**
Scale	**3-4 million individuals, mostly in larger schemes and numbers likely to decline.**	

6.1.4 Equity Release

The equity release market has undergone considerable change in recent years due in large part to media and consumer group pressure and appropriate regulatory responses. Were we producing this chart in the 1980s, it would have been very red. We suggest that the probability of detriment remains orange but there is a recognition that as FSA requirements bed down and inappropriate sales techniques are weeded out, concerns may ease further. A continued regulatory focus on the market is needed as mortgage brokers turn to equity release as an alternative revenue source in the current market.

Figure 13: Analysis of detriment in equity release market

Equity Release	Materiality of detriment	Probability of detriment
Inappropriate products / risks	**Some consumers sold equity release where inappropriate**	**Reduced by sales regulation but concerns about misselling continue**
High charges / costs	**High interest rates can rapidly reduce equity in property.**	**Little evidence that charges inappropriate for the risks involved.**
Emotional / psychological	**Concern about keeping home or retaining flexibility. Loss of ability to leave assets to family.**	**Changes in product, FSA regulation and self-regulation by market reducing risk. Loss of inheritance ability continues to play a role.**
Scale	**A small market at present**	

6.2 *Protection*

6.2.1 Life insurance and funeral plans

Overall there is limited evidence of detriment in the life insurance and funeral plans market. Since the introduction of regulation in 2001, the funeral plan market is more tightly regulated and consumers have more security that their money will be available when the time comes. The life insurance market is directly regulated by the FSA and has well established processes for seeking redress if required. Given the wide variety and variation of products available in both the life insurance and funeral plans markets, it is important that buyers read the terms and conditions of their plans/policies carefully so that they are clear about what is included and excluded. Even by doing this there is still the possibility (in the case of insured plans) of detriment occurring where people pay more in premiums that will be paid out on their death or that the cost of a funeral exceeds the sum of life assured.

Figure 14: Analysis of detriment in Life insurance market

Life Insurance	Materiality of detriment	Probability of detriment
Counterparty risk	**Due to collapse of insurer /funeral director**	**Reduced by regulation and compensation schemes**
Inadequate / excess cover	**Family can still be left with money to pay**	**Funeral costs outstripping inflation**
Remedial costs	**Process likely to be straightforward**	**FOS, FSCS procedures well established FPA procedures in place**
Emotional / psychological	**Interventions in place to prevent likelihood of occurring**	**No evidence found of detriment occurring**
Scale	**Approximately 75,000 pre-paid funeral plans sold each year and growing at 11%pa. Estimated insured market growth of 20-25%.**	

6.2.2 Income protection

No evidence was found to indicate that there is a market for income protection beyond 70 years of age and therefore there appears to be no detriment in this market.

6.2.3 Medical expenses insurance

Based on the findings of the Experts' Working Group report on age discrimination in financial services, this is viewed as a market where little detriment exists and where older customers are well served. Whilst some consumers may find the costs of medical cover too high for them to afford, there is no evidence that premiums are disproportionate to the costs involved.

6.2.4 LTC insurance and immediate needs annuities

The absence of a significant LTC insurance market is the main cause of detriment as cover is unavailable for those who may want it. With only two providers there is limited scope to compare quotations. However, with the forthcoming Green Paper on funding of social care may come further changes in the market.

Figure 15: Analysis of detriment in immediate need annuity market

Immediate needs Annuities	Materiality of detriment	Probability of detriment
Counterparty risk	**Due to collapse of insurer**	**Reduced by prudential regulation and FSCS – could be of concern if provider is too specialised in this market.**
High charges / costs	**Limited competition could result in high prices**	**No evidence that market inefficient**
Remedial costs	**Process likely to be straightforward**	**FOS, FSCS procedures well-established**
Opportunity costs	**Lack of LTC market leads to risk of running out of funds for care**	**At present, lack of market makes this risk moderate to high for some, moderated by average short length of stay in care.**
Societal burden	**Costs fall back on State**	**Constrained to some extent by means testing and tightening of eligibility criteria**
Emotional / psychological	**Some concern over loss of leaving inheritance**	**Offset by certainty of payment of care home fees**
Scale	**A small market but many millions face the prospect of needing care and finding funds. If a social insurance fund is introduced, the market will become very large overnight.**	

6.2.5 Longevity insurance

As noted in section 5.2.3 above, there are currently no products available on the market in the UK to protect individuals from living too long and running out of funds (other than traditional annuities described in the decumulation section above). In the current economic climate, it is unlikely that a product will be launched in this market in the short term due to a number of factors such as the level of capital required, the lack of financing opportunities for insuring against longevity risk. Detriment exists only to the extent that there may be demand for such products but no supply.

6.2.6 Travel insurance

Some evidence of consumer detriment exists with older people experiencing difficulty in obtaining quotations for travel cover. This is more evident among those aged 75 plus years who are more likely to be refused cover. There is a wide disparity in prices for comparable cover making it difficult for an individual to be assured that they have found the best value for money when insurance is obtained.

Existing interventions such as the FSA's financial capability initiative and Money Made Clear information source provide limited assistance in helping the individual determine where to go to get the best value for money that meets their needs. Some third sector and commercial organisations target older people and are more likely to provide appropriate cover taking age and health into consideration. Third age organisations hope that the secondary legislation relating to financial services in the Equality Bill will make it easier for older people to obtain quotations for travel cover and that prices differentials will be proportionate to the actual risk.

Figure 16: Analysis of detriment in travel insurance market

Travel Insurance	Materiality of detriment	Probability of detriment
Loss of cover	**Due to collapse of insurer**	**Reduced by prudential regulation and FSCS**
High charges / costs	**Age discrimination = higher prices?**	**More competitive pricing available from specialist providers**
Inadequate / excess cover	**Travel without cover or not fully insured**	**Research indentifies that people will travel without full cover**
Opportunity costs	**Costs incurred by travelling without cover**	**Access inadequate especially among 75+**
Emotional / psychological	**Restricted lifestyle**	**People generally accept limitations that come with age**
Scale	**Estimated 6.5 million people aged 65 and over travel at least once a year.**	

6.2.7 Motor Insurance

Some evidence of consumer detriment exists with older people experiencing difficulty in obtaining quotations for motor cover, particularly when trying to rent a car. It is difficult for older motorists to shop around for competitive premium as only a limited number of insurers will take new older customers. Access to insurance rather than cost is a more significant issue.

Existing interventions such as the third sector and commercial organisations who target older people, signposting to BIBA (British Insurance Brokers Association) by some insurers and the increasing availability of alternative and in many cases, subsidised travel reduce the potential for detriment in this market.

Figure 17: Analysis of detriment in motor insurance market

Motor Insurance	Materiality of detriment	Probability of detriment
Loss of cover	**Due to collapse of insurer**	**Reduced by prudential regulation and FSCS**
High charges / costs	**Age discrimination = higher prices?**	**Perception rather than reality**
Inadequate / excess cover	**Auto-renewal may mean unnecessary cover retained – multiple drivers**	**Compulsory 3rd party Key Facts document**
Opportunity costs	**Cost of alternative travel**	**Most people can get cover**
Societal burden	**Cost of subsidised travel**	**Reduces potential for social isolation**
Emotional / psychological	**Social isolation - lead to depression, lack of access to services**	**Number of Local Authority transport plans /strategies in place with focus on accessibility for older people**
Scale	**Over 15 million driving licence holders aged 50+, of which 1 million is over age 70.**	

6.2.8 Home insurance

No significant gaps in the home insurance market were found as older people tend to pay less for insurance. Potential detriment among low income households is being addressed through the work of the DWP Financial Inclusion team, the ABI and social landlords working together to facilitate cover through tenants contents insurance schemes.

6.3 Banking and credit

6.3.1 Bank accounts

Among the majority of the older population, there is little evidence of consumer detriment in the bank account market. Potential detriment is more likely to occur among those who are unbanked or are on the margins of banking. However, the initiatives from the financial inclusion team continue to reduce the potential of detriment occurring.

Figure 18: Analysis of detriment in banking market

Bank accounts	Materiality of detriment	Probability of detriment
Loss of capital	**Due to collapse of bank**	**Reduced by prudential regulation and FSCS and by growing consumer awareness of need to spread funds.**
Remedial costs	**Process likely to be straightforward**	**FSCS scheme well established**
Opportunity costs	**'Poverty premium' arising from increased financial transaction costs**	**Basic Bank Accounts have reduced potential detriment**
Emotional / psychological	**Stress and anxiety relating to security of cash** **Reduced confidence in using technology for financial management**	**Financial inclusion initiatives, support and championing from third sector organisations**
Scale	**Majority of 20 million 50+ market have a bank account**	

6.3.2 Credit

Regulatory interventions requiring lending organisations to assess an individual's ability to pay significantly reduce the potential for detriment among older consumers in this market.

Figure 19: Analysis of detriment in credit market

Credit	Materiality of detriment	Probability of detriment
High charges / costs	**Higher interest rates due to poor credit rating using non mainstream providers**	**Occurring where original debt is not paid off**
Opportunity costs	**Loss of income in servicing loan**	**Reduced by regulation (illegal sources excluded)**
Societal burden	**Potential for increased dependency on state benefits**	**More likely to occur on margins and among existing benefiters**
Emotional / psychological	**High level of anxiety relating to ability to repay**	**In extreme cases, (attempted) suicide may occur**
Scale	**Almost 5 million over 50s have either outstanding credit on their cards or some other kind of debt**	

6.3.3 Mortgages

The potential for detriment is low in the mortgage as most homeowners will have paid their mortgage at or near retirement. Regulatory interventions such as the FSA's MCOB (Conduct of Business rules) and 'Guidance on Mortgages Running into Retirement' provide lenders clear guidelines on assessing affordability to older customers.

6.4 *Saving & Investment*

6.4.1 Savings accounts

The combination of insolvent banks and building societies needing rescue combined with the lowest interest rates in living memory has served to highlight the potential for consumer detriment in this market. Consumer awareness of the options available to them to secure an income through an annuity remain low, although demand would in any event be tempered by the desire to leave money to family. Raising awareness of alternative approaches to generating an income, particularly in much later life could reduce the scope for detriment.

Figure 20: Analysis of detriment in savings account market

Savings accounts	Materiality of detriment	Probability of detriment
Loss of capital	**Loss very significant for those dependent on savings**	**Reduced by prudential regulation and FSCS and government intervention and by growing consumer awareness of need to spread funds.**
Loss of income – inappropriate product	**Those reliant on income from savings may have the wrong product and should not be taking interest rate risk**	**No requirement to assess suitability of holding money in cash and many unaware of alternatives.**
Opportunity costs	**For some, the purchase of an annuity may have protected their income**	**Many with cash savings may never have access to advice on how best to protect their income**
Remedial costs	**Process likely to be straightforward**	**FSCS scheme well established**
Societal burden	**Some individuals may fall back on state benefits as they deplete capital**	**Moderated by consumers making do with a lower income**
Emotional / psychological	**Stress and anxiety relating to security and level of savings and income levels.**	**Moderated by actions of government and compensation scheme.**
Scale	**Majority has some form of savings account**	

6.4.2 Mortgage endowments

In recent years, there has been considerable evidence of detriment in the mortgage endowment market with many consumers exposed to risks that they did not understand. Many consumers have now been compensated for losses incurred and most consumers with mortgage endowments have restructured their mortgages to ensure that they are paid off. However, some of those reaching retirement soon may still find themselves with inadequate resources to pay off their mortgages at retirement.

6.4.3 Investment Bonds

Consumer risks lie mainly in high charges and inappropriate risks. Whilst these should be reduced through sales regulation, there remains some evidence of unsuitable sales.

Figure 21: Analysis of detriment in investment bond market

Bank accounts	Materiality of detriment	Probability of detriment
Loss of capital	**Insolvency of insurer could lead to loss of funds**	**Reduced by prudential regulation and FSCS**
High charges	**Impact can be significant over time.**	**No up-to-date evidence for higher costs other than anecdotal**
Inappropriate risks	**Risk averse consumers sold products whose risks they do not understand**	**Continued but anecdotal evidence that misselling occurring.**
Remedial costs	**Process likely to be straightforward**	**FSCS scheme well established**
Emotional / psychological	**Stress and anxiety relating to unexpected losses**	**Examples continue to be quoted by media**
Scale	**Small market but concentrated among those in later life**	

6.4.4 Unit Trusts / Investment ISAs

There are few examples of misselling of traditional unit trusts or investment ISAs but recent headlines suggest that risk averse older consumers can be at risk of being sold high risk products. Suitability rules and pressure from the FSA to compensate such customers can help to address financial loss but less can be done about the emotional stress that may result.

6.4.5 Structured Products

The main concerns with this market lie in the high charges and the exposure to risks for some consumers. However, there is little evidence that detriment is widespread.

Figure 22: Analysis of detriment in structured product market

Structured products	Materiality of detriment	Probability of detriment
Counterparty risk = loss of income	**Insurer insolvency could leave consumers with reduced capital / income**	**Reduced by prudential regulation and FSCS but some uncertainty over risks to providers**
Exposure to poorly understood risks	**Loss of capital / income could be high due to risks inherent in some products**	**Reduced by sales regulation and previous scares**
High charges / costs	**High charges can significantly reduce benefits of guarantees and/or flexibility.**	**Some uncertainty about levels and impact of charges.**
Remedial costs	**More complex products – lack of suitability may be harder to prove**	**FOS, FSCS procedures well-established**
Emotional / psychological	**Concern about impact of economic and stock market conditions**	**Guarantees should protect against undue stress**
Scale	**A small market**	

6.5 Information, Guidance and Advice

The failure to be able to access appropriate information, guidance or advice can ultimately lead, in the extreme, to poverty and social exclusion in later life. Whilst no studies have fully evaluated the extent to which this exists, there appears to be significant evidence of a gap in supply which the FSA, other agencies and the third sector are seeking to narrow, but with limited resources. We suggest that there is likely to be considerable unmeasured detriment among those in later life due to their limited access to financial help.

Figure 23: Analysis of detriment in information, guidance and advice

Bank accounts	Materiality of detriment	Probability of detriment
Inappropriate product choices	**Older consumers less able to recover from poor choices**	**Financial capability data suggests ability to choose products falls with age**
Missed opportunities	**Those in later life 'make do' rather than seek out advice**	**Several reports suggest that needs for information and advice are not being met**
Emotional / psychological	**Stress and anxiety particularly among those with limited access to help**	**Needs not matched by supply and emotional loss likely**
Scale	**Most older people require information, guidance or advice at some point in their later years.**	

7 Opportunities for the Consumer Panel

This initial, wide-ranging analysis of later life and financial services suggests that the subject is one worthy of further consideration, research and activism by the FS Consumer Panel and by other industry and third sector groups; indeed many organisations are already looking at different aspects of this issue. The Panel has the advantage of being able to look at the issue holistically from the consumer perspective and as an independent consumer body.

The issues facing those in later life in trying to manage their finances effectively are likely to become more complex rather than easier as we move towards a society where more of the responsibility for funding retirement and long-term care is passed to the individual. Furthermore:

- The decisions made in later life are complex, critical, sometimes stressful and irreversible, and often are unlike decisions made in earlier life;
- Products are themselves complex and varied, and subject individuals to very different levels of risk and opportunity, and in some cases, high charges;
- Information, guidance and advice remains in short supply and of varying quality;
- Some older consumers are often vulnerable to sales pressure, crime and abuse, whilst many may find it difficult to gain access to suitable information and advice and are in some cases excluded from markets. Some may not have the capacity to make informed decisions, even with access to appropriate information and advice.

The scope for significant consumer detriment arises in most markets, although the materiality of that detriment appears greatest in decumulation markets, saving and investment markets and information, guidance and advice. However, the probability of detriment is reduced or mitigated by existing or forthcoming interventions. Several instances of legislation, regulation or industry intervention have been identified which seek to remove, reduce or compensate for detriment. Clearly those that remove or reduce detriment are preferable to retrospective compensation.

We consider in more detail below whether this market sector meets the Panel's own prioritisation criteria; the case for action and prioritise where action could be focused and outline a strategy for the Panel to move forward with this issue.

7.1 Are the Panel's criteria met?

As noted earlier, the criteria used by the panel to determine whether a matter should be prioritised as one which the Panel should develop work on are:

- Is it a consumer issue? Both individuals and their wider families are affected by financial decisions (and non-decisions) made in later life. The later life sector meets this criterion;
- Is there actual or potential serious or widespread consumer detriment? Whilst this scoping study suggests that the potential for detriment is more widespread than actual detriment, there is evidence that where detriment does occur it can be extremely serious in nature, sometimes resulting in a serious loss of capital and income in later life, and/or in some markets widespread with large numbers of individuals affected by lack of access to markets such as travel insurance;

- Does the Panel have the capacity and resource to get involved? The resources available to the Panel clearly limit the role which it can take. However, given the nature of the risks to which those in later life are exposed, we argue below for the panel developing a clear strategy for addressing this market. We leave it to the Panel to determine precisely what level of resource it does devote to this sector;
- Are other bodies involved on the same side? As we point out throughout this report, there are many organisations undertaking research, developing initiatives or addressing detriment directly. However, there is a tendency for individual organisations to be focused on particular aspects of the sector rather than the sector as a whole. The exception to that rule may be the merged Age Concern / Help the Aged organisation. We suggest that the subject of later life is such a large one that there is scope and justification for another organisation such as the Panel committing resource to examining the sector holistically or in a cross-cutting role;
- Will Panel intervention make a difference? Clearly this question is a difficult one to answer. The Panel has considerable influence in those markets regulated by the FSA and its voice as a more general consumer campaigner carries weight more widely. Many of the markets and issues identified for focus in this report are FSA regulated markets which would suggest that intervention should make a difference.

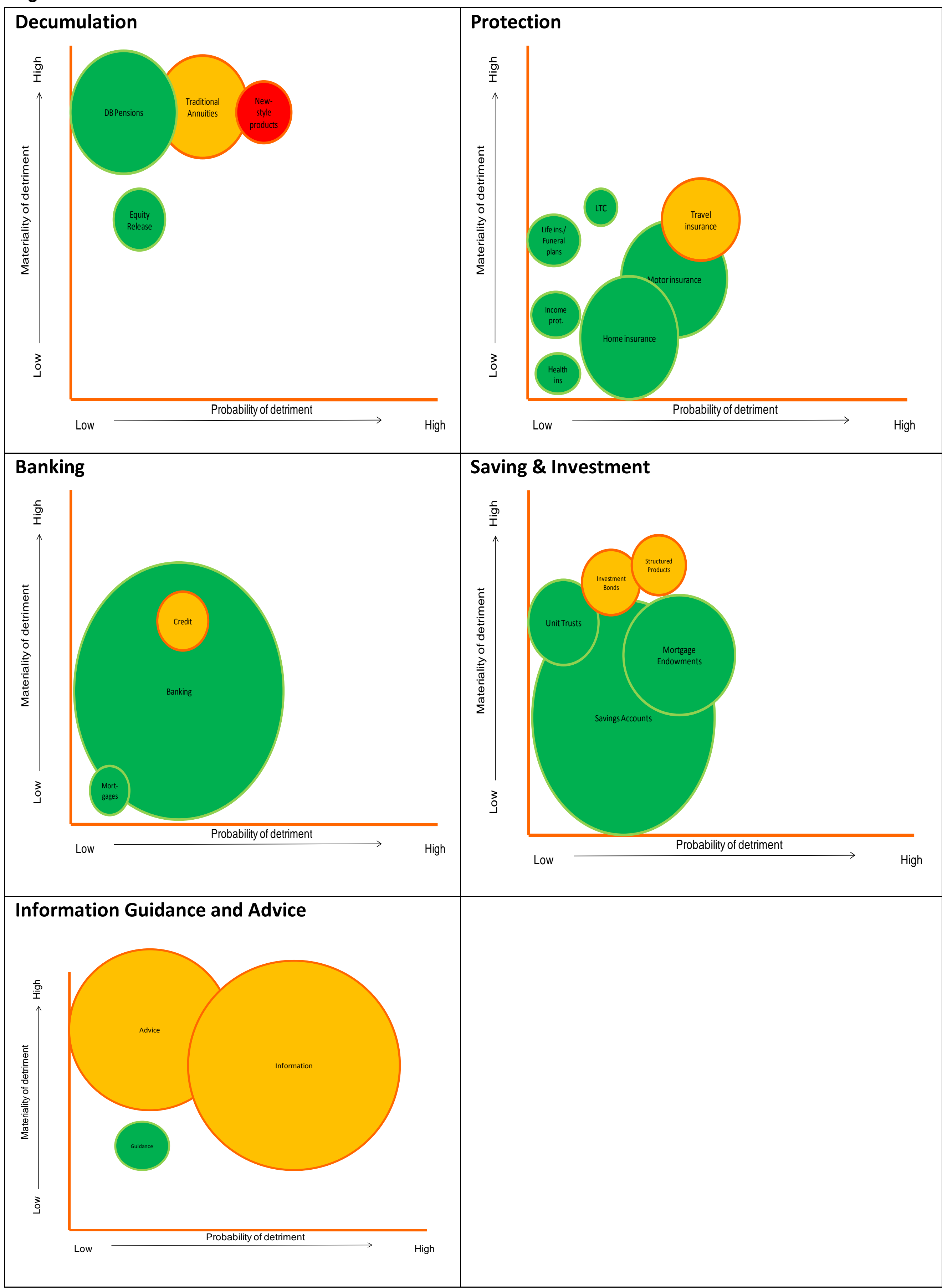
7.2 Where should the Panel focus its strategy?

Whilst there are a number of overarching issues facing those in later life – managing risk; managing lifestage transitions; managing ill-health, managing bereavement, all of which impact on an individual's financial position, it is also the case that some markets warrant more attention than others.

The charts below (Figure 24) are illustrative only and are not intended to measure with any precision the materiality or probability of consumer detriment in each market. Rather they seek to highlight those market sectors where detriment may be most significant or possible in today's environment (highlighted in red or yellow in the charts) and where the Panel may choose to focus its work. The size of the bubbles in the charts is an indication of the relative size of markets, although the nature of the shapes and words means that very small markets are difficult to show small enough in relation to very large markets, in other words, proportions are not exact.

In the decumulation market, two products stand out (in red or yellow). In the case of new-style annuities, there is little current evidence of (and no research) on detriment but concerns about consumers being missold such products and whether the products represent good value for money have been raised in recent times. Traditional annuities, whilst a much larger market is one where several areas of consumer detriment are being addressed but concerns about the lack of joint life annuities continues to be of concern. Given the importance of these products in helping consumers maintain their income in retirement, the detriment were it to arise could be very significant for both the individual and society.

Figure 24: Sectors most at risk of detriment.



In the traditional annuity market, whilst current initiatives can be seen to be reducing detriment, concerns still exist about levels of consumer understanding and the type of annuity being purchased. Broader concerns have been raised about the ability of advisers in this market to deal with the growing complexity of products on offer. Whilst DB pensions exhibit the potential for significant consumer detriment and concerns about the long-term sustainability of the PPF, at the present time, the probability of detriment appears to be quite low. The risk to the insurance sector from improving mortality continues to be highlighted by the FSA and the FSA industry should continue to be encouraged to monitor improvements brought about by biomedical advances.

By contrast, whilst there are a number of issues in the protection market that warrant further attention, the materiality of any detriment is likely to be less than in the decumulation market. The money at risk is less and any emotional detriment is likely to be proportionately less, although it is important not to play down the sense of social exclusion that can result from limited access to insurance products that facilitate mobility. Of all the markets, travel insurance would appear to be the one which warrants some attention from the panel.

In the banking sector, several initiatives are at work to reduce the detriment suffered by older people, notably the work of financial inclusion. However, the credit market remains one where potential detriment can be high for those few who find themselves with high levels of debt in later years of life. Inability to repay debt in later life can lead to very significant levels of stress with a knock-on effect on health and social inclusion.

In the savings and investment markets, the risks and costs of structured products and investment bonds continue to warrant attention, particularly in today's difficult market conditions. Asymmetry of information, high charges and complexity of risks can easily lead to the risk of misselling.

In theory, all those in later life will need information, guidance and/or advice at some point. However, for those who are financially capable or have a strong family or social network or have a relationship with a financial adviser the question of where and who to turn for information and/or advice may be less of an issue, though some may suffer detriment from poor advice. The potential for detriment is greater among those who do not know where to go for information and/or advice and lack the capability to fully understand the implications of the decisions that they might/might not take as a consequence. With the exception of those who fall within the remit of financial exclusion, it is difficult to identify exactly how many later life consumers could and do suffer detriment in this area.

The above analysis suggests that the Panel may choose to prioritise their work on later life in the following order:

1. Decumulation markets;
2. The provision of Information, Guidance and Advice
3. Savings & Investment markets;
4. Protection markets;
5. Banking markets.

7.3 A way forward for the Panel

In considering a strategy for the FSA we are guided by two factors: what role is appropriate given the Panel's terms of reference, and what the Panel is able to do with its limited resources. The panel is clearly not able to resolve any of the potential detriment through direct consumer action; it is neither resourced nor empowered to deal directly with consumers. We have also ruled out any major research initiatives (although there are some areas where the Panel may be able to devote some resource to further research). This leaves the Panel with options which range from maintaining a watching brief, through further research and into more active recommendations to regulators, in particular the FSA, industry, the Government and the third sector.

Our recommendations for the Panel are that it should consider adopting a strategy which includes the following elements:

5. The panel should consider making Later Life and Financial Services one of its key consumer-oriented areas of focus (as opposed to focusing on specific market sectors). A specific working group could be convened to review on an on-going basis the broad range of issues facing those in later life and to consider whether the risks of detriment in any of the markets in which older people participate have been reduced or increased by interventions or market behaviour. The focus of the working group in the early years should be decumulation, savings and investment markets and Information, Guidance and Advice, but with a watching brief on developments arising from the Equalities Bill and developments in the credit market.
6. The Panel should consider adopting a cross-cutting role in helping to develop and shape a holistic view of the consumer in later life and encouraging further research. The Panel could leverage its independent position as a consumer group in financial services to engage with a wide range of interested parties including Government, regulator, industry, think-tanks and third sector. Particular areas of focus could include:
    a. The implications of the Green Paper on the funding of social care for older consumers and the industry;
    b. Developments occurring in response to the Equalities Bill, in particular reviewing the outcome of current research projects investigating the financial services sector;
    c. Review of forthcoming research on decumulation to develop a holistic view of the emerging issues (if any) and encourage further research in these by the contributors if appropriate.
7. In many areas of the market, research has either been completed recently or is underway. However, in areas where uncertainties remain, the Panel should consider whether it can be effective in commissioning further research. Areas which would appear to justify further research include:
    a. The pricing and risks of alternatives to traditional annuities - do they represent good value for money? What opportunities and risks that they represent for consumers?
    b. The delivery of financial information, guidance and advice to those in later life – what are the needs of those in later life, are there ways in which advice can be delivered in a safer environment and with greater accessibility? How can the supply of advice be increased in an appropriate way?

c. The Panel may wish to explore whether the Banking Code adequately deals with the risks associated with bank and building society accounts and whether these are adequately disclosed to and understood by consumers.

Alternatively, if resources are limited, the Panel might consider encouraging other parties to commission research or forming a consortium to investigate these issues.

8. The Panel should construct a short list of issues to address back to the FSA. Our suggestions include:

   a. Decumulation. Are the risks to insurers and consumers of the new 'third way' decumulation products clearly understood in respect of solvency and suitability? Are the risks to annuity providers from medical advances fully understood and factored into pricing?

   b. Later Life advisors - Are the standards of qualification and ethics for advisers to those in later life adequate and sufficiently well defined? Do existing examinations prepare advisers adequately for dealing with new-style decumulation products? Is there a need to set out a distinct set of ethics for the way in which advisers deal with more vulnerable consumers, including those in later life? Is there a need for guidance on the attitudinal / psychological profile of advisers suitable for dealing with those in later life (or by contrast, a profile of those unsuitable for dealing with older customers)? Is there a need for any additional training to be provided to advisers dealing with older customers to make them aware of the significance of advice to those in later life? All of these questions could be directed to those dealing with professionalism within RDR.

   c. Financial Capability - Can the FSA report on the progress of its financial capability strategy for those in later life? Has the Money Guidance / MoneyMadeClear Pathfinder been successful in reaching and providing guidance to those in later life and what needs have been identified? Is there a view emerging as to whether the Pathfinder is successful in helping people to reafch successful outcomes?

In summary, we believe that there is a strong case for the Panel to further review and take up a number of issues relating to later life and financial services We suggest that the Panel considers implementing a four-part strategy based on review, engagement, research and constructive dialogue will help to identify and clarify any significant new detriment and help to drive forward solutions for addressing current concerns.

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