

A collection of perspectives

DP16/1

# Ageing population and financial services

February 2016



Financial Conduct Authority



We are asking for comments on this Discussion Paper by Friday 15 April 2016.

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# Ageing population and financial services

February 2016

## **Disclaimer**

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# Foreword



**Tracey McDermott**  
Acting Chief Executive  
Financial Conduct Authority

In the UK, the average life expectancy of children born in 2013 is over 90 years old, and the number of people aged over 65 already outnumbers those under 16.<sup>1,2</sup> This changing demographic is driving, and will continue to drive, a need for new and different financial products and services to meet the needs of our ageing population. This provides both opportunities and challenges for firms across the financial industry. It is critical that our financial services markets are able to adapt to meet these needs.

Our aim with this programme is to work collaboratively with others to help bring about positive change. It is not the role of the FCA to design the products required or define how they should be delivered. But we do believe we have a role to play in helping to facilitate the debate about what older people need from financial services providers and the barriers that might get in the way of delivering them in a way that is accessible to those consumers.

***Our aim with this programme is to work collaboratively with others to help bring about positive change.***

Financial services provision is, of course, only a small part of what might improve outcomes for the ageing population. Many of the most difficult problems that older consumers face, such as issues regarding consumers' health or cognitive ability simply cannot be solved by financial services.

However, we do believe that older consumers' lives can be made easier by more effective provision of appropriate financial products and services which help them to manage these risks and, for example, to fund longer periods of retirement.

So we are approaching things a bit differently with this piece of work. This Discussion Paper is a collection of think pieces by different interested parties and is intended to provoke discussion and debate about how financial services work for older consumers. Our aim is to ensure that consumers have access to products and services that are well-governed and deliver value

for money in competitive markets. We will use this Discussion Paper to build on existing work we have underway, including that on changes in the pensions market, how financial advice is delivered and consumers in vulnerable circumstances.

We will continue to work with others to identify the challenges facing older consumers now and in the future. We value external perspectives and engagement, and I would encourage you to contact our Ageing Population team (details on page 66) if there are specific areas

where you believe change is needed. We want to create a regulatory environment that encourages good market outcomes, and we cannot do this without insight from experts from across the spectrum.

- 1 [www.ons.gov.uk/ons/re/lifetables/historic-and-projected-data-from-the-period-and-cohort-life-tables/2012-based/info-surviving-to-age-100.html](http://www.ons.gov.uk/ons/re/lifetables/historic-and-projected-data-from-the-period-and-cohort-life-tables/2012-based/info-surviving-to-age-100.html)
- 2 [www.ons.gov.uk/ons/re/pop-estimate/population-estimates-for-uk-england-and-wales-scotland-and-northern-ireland/mid-2014/sty---overview-of-the-uk-population.html](http://www.ons.gov.uk/ons/re/pop-estimate/population-estimates-for-uk-england-and-wales-scotland-and-northern-ireland/mid-2014/sty---overview-of-the-uk-population.html)



# Introduction



## Linda Woodall

Director of Life Insurance and Financial Advice  
and Sponsor of Ageing Population Project  
Financial Conduct Authority

People are living longer lives on an unprecedented scale. In the next five years, the number of consumers aged over 65 in the UK is expected to increase by 1.1 million, and the proportion of people aged over 100 will rise by 40%.<sup>3</sup> And it is well established that those aged 85 and over represent the fastest growing segment of the UK population. Demographic change is at the heart of the challenges posed by the ageing population. Regulators and firms need to adapt to make sure that financial services are still fit for purpose, and able to meet the wide range of needs of today's older consumers.

To establish whether our regulatory settings are in the right place, we first need to ensure that we understand the complex range of issues and opportunities at play for older consumers. Financial services should genuinely meet the changing needs of older people, at every stage of later life. I am leading a new team at the FCA that is looking specifically at the challenges facing the ageing population and financial services. We are conducting a programme of research and stakeholder engagement to deepen our understanding about how markets work for older consumers, allowing us to make recommendations that improve outcomes for these cohorts.

One thing we do know is that one size does not fit all. Older consumers are a diverse population, with different beliefs, behaviours and needs, all of which affect the way in which they interact with money and financial services. Within diverse groups of consumers, an individual's needs and attitudes can change over time. While someone retiring in 1965 would have expected to enjoy only a few years of retirement, (with the average life expectancy in the UK at just under 72), now it is not uncommon for retirement to last two to three decades.

While life expectancy is improving, there are some trends which we should not ignore. As we age, we are

increasingly likely to suffer with health conditions and this brings forward a number of challenging issues, such as the provision of long-term care, handling cognitive decline, and ensuring appropriate access channels are available to those that need them.

Evidence also suggests that as we age we tend to rely less on reasoned, deliberative thinking and more on gut-feel and things learned through experience. Older people also find it more difficult to navigate the proliferation of choice. This emphasises the importance of framing products and services in a way that meets the needs of older people.

We also need to be mindful that older consumers can sometimes become vulnerable consumers, as shown in the FCA's previous work on consumer vulnerability: every consumer runs the risk of becoming vulnerable due to their personal circumstances, no matter what their age.<sup>4</sup>

We know that it is important to understand the characteristics of different consumer groups in any given population, as this is what allows us to monitor whether financial services effectively meet their needs. At the FCA, we have already done some work to segment consumers through our Consumer Spotlight model.<sup>5</sup> As part of this project, we are looking at a more in-depth segmentation of older consumers, so we have a more detailed understanding of older people's needs and characteristics. We acknowledge that the overall financial health of any consumer can, in itself, be complex, and many consumers may have wealth tied up in assets that are not easily liquidated, such as property. By using research to understand more about the types of consumers that make up the UK population, we will be able to use our regulatory toolkit to encourage markets to adapt where necessary.

We have launched our work on the ageing population with a Discussion Paper featuring contributions from a range of interested individuals and organisations because we know that the FCA can only be part of the solution to the myriad of issues raised. The purpose of the paper is to stimulate debate about how the financial services industry can better meet the needs of our ageing population. The views expressed in this paper are the authors' own and show some of the breadth and complexity of the issues relevant for older consumers. We recognise that the topics discussed in this paper are not comprehensive and we would like to hear from other experts to enhance our understanding of the issues and opportunities to improve markets for older people, particularly on areas not covered by the contributions.

I would like to thank everybody who has contributed to this paper and to the debate so far. This paper is intended to provide a snapshot of some the issues and opportunities relevant for the ageing population, and we look forward to discussing these further as our work progresses. Collaborative engagement is key and we

look forward to working together with firms and other stakeholders to promote better markets in the future.

In addition to this paper, we are developing a programme of work that will look at key issues for the ageing population in more depth. This programme will include a series of roundtables and bilateral meetings with stakeholders, research of the key issues, and subsequently, development of recommendations that form a regulatory strategy for the ageing population. Finally, I would like to echo Tracey's invitation for collaboration: we would like to work together with our stakeholders to develop and deliver a range of better outcomes for older consumers. I invite contributions on areas where you believe that positive change could be made.

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3 [www.parliament.uk/business/publications/research/key-issues-parliament-2015/social-change/ageing-population/](http://www.parliament.uk/business/publications/research/key-issues-parliament-2015/social-change/ageing-population/)

4 'A vulnerable consumer is someone who, due to their personal circumstances, is susceptible to detriment, particularly when a firm is not acting with appropriate levels of care.' FCA, Consumer Vulnerability Occasional Paper, February 2015

5 [www.fca-consumer-spotlight.org.uk](http://www.fca-consumer-spotlight.org.uk)

***Older consumers are a diverse population, with different beliefs, behaviours and needs, all of which affect the way in which they interact with money and financial services.***





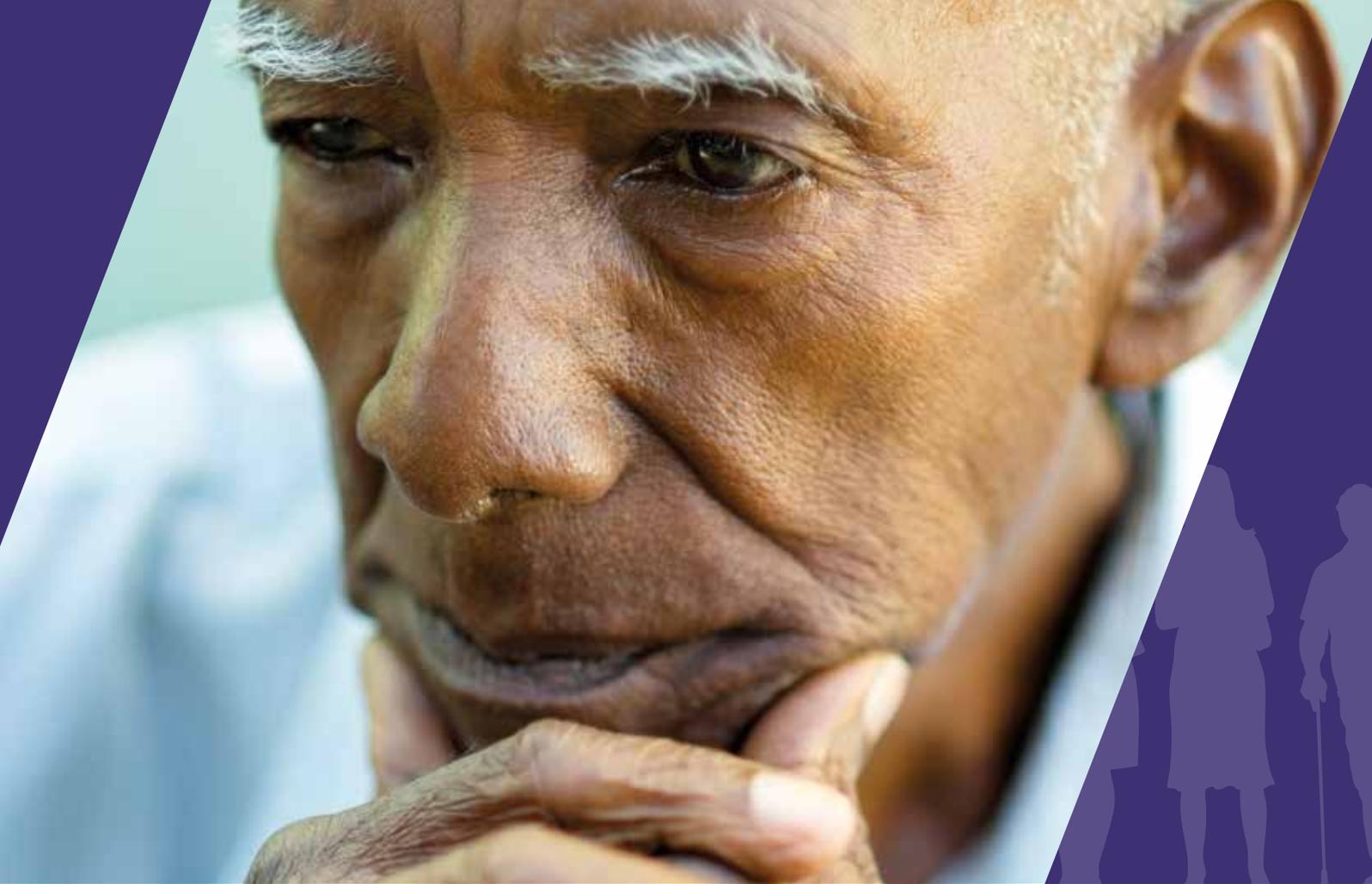
## Next steps

To complement this Discussion Paper, we are conducting a research and literature review and an in-depth consumer segmentation of older people. We will combine this with our own analysis of current regulatory priorities to focus the scope of the project on particular issues within financial products or services.

We want to work collaboratively to drive better outcomes for consumers and we will continue to engage with our stakeholders on key issues. We will supplement the information gathered through this Discussion Paper and stakeholder engagement with further research, which will be scoped in the second quarter of 2016.

All of this work will help us to develop an FCA Strategy on the Ageing Population, which we will launch in 2017. This strategy will make recommendations about how we can improve outcomes for older people, including whether regulatory settings need further review.

At this stage, the scope of the project is wide, and we are interested in understanding more about how financial services operate for all consumers aged 55+ across all financial markets. In due course, we expect to narrow the focus of this project as a result of insights from our stakeholders, further research and analysis.



## What can you do?

If you are interested in some of the ideas raised in this Discussion Paper, or have further views you would like to share with us, please get in touch with the Ageing Population team. The deadline for responses is Friday 15 April 2016 and we are open to receiving any comments that are relevant to the scope of this project.

Specifically, we would like to invite comments that include suggestions of areas for further focus by the FCA, which are evidenced where possible. Comments of this nature will help us to prioritise areas for further work. We are particularly interested in comments on markets that have not been widely covered by the contributions to this Discussion Paper.

To respond to this Discussion Paper, please see Annex 1.

## What will we do?

We will consider your feedback and publish a Feedback Statement as part of our wider Strategy for the Ageing Population, expected in the second quarter of 2017.

This Discussion Paper is intended to stimulate debate, and launches a programme of work at the FCA. We will continue to engage with our stakeholders about the Ageing Population through a series of roundtables in the second and third quarters of 2016, and ongoing bilateral engagement.



# **1. How older consumers assess their own needs**



**By Nigel Keohane**  
Research Director  
Social Market  
Foundation

## How can we stop pensioners from underestimating their longevity and running out of money?

The UK pensions' landscape changed dramatically on 6 April 2015 following the implementation of the 'freedom and choice' reforms. Before, there was an effective requirement to buy an annuity with Defined Contribution (DC) savings and thus insure against longevity risk; now, pensioners can spend their savings as they wish.

As the FCA has acknowledged, 'sustainability of income' is an especial concern in this new environment.<sup>6</sup> Will people's pension savings last them through the long retirements that many will now experience?

Perhaps unsurprisingly, given increasing longevity, people aged 50–60 on average underestimate their life expectancy – men by two years, women by four years. The Institute of Fiscal Studies notes that, in particular, too few people expect to live until very old age.<sup>7</sup> Research has also found that many retirees have to be prompted before they even consider longevity risk in their retirement planning.<sup>8</sup>

These cognitive and behavioural traits are likely to be important. Underestimating life expectancy may affect the product choice that a retiree makes – by making annuity rates appear poorer value than they are in actuality. For retirees pursuing income drawdown in retirement, underestimating life expectancy may result in the person spending their savings too quickly.

The effects are also unlikely to be felt evenly. For instance, women are currently exposed to more acute longevity risks than men because they retire earlier on average (63 compared to 65 for men) and live for longer (age 89 rather than 87 for men).

While it is too early to tell whether these risks are materialising in the UK, as the Social Market Foundation's recent report *Golden Years?* showed, international evidence suggests that the risk of running out of money is real though far from universal.

In comparator countries that have similar pension freedoms, very few individuals buy an annuity (5% in Australia and 10% in the USA), way below the historic rate in the

<sup>6</sup> FCA, 'Pension reforms – proposed changes to our rules and guidance' (2015)

<sup>7</sup> IFS, Rowena Crawford and Gemma Tetlow, 'Expectations and experience of retirement in Defined Contribution pensions: a study of older people in England' (2012)

<sup>8</sup> Ignition House (for the FCA), 'Exploring consumer decision-making and behaviour in the At-Retirement landscape' (2014)

UK (75%).<sup>9</sup> The evidence also reveals considerable variation in decumulation patterns. Interestingly, the average (mean) behaviour in Australia is a cautious one, preserving capital by reducing wealth by less than 1% a year. Alongside this, a significant minority spend their pension savings quickly, with one in four running out by age 70 and an estimated four in ten run out by age 75. In the USA, of those who draw down on their pension savings, the average rate of withdrawal is 8% per year.

Applying these behaviours to UK retirees illustrates some of the risks associated with the pension freedoms:

1. UK retirees following the cautious Australian decumulation path face a very low risk of running out of savings, even if they live longer than average. But, the downside is comparatively low incomes. This exposes the fact that by self-insuring against longevity risk, individuals must plan to stretch their retirement savings across their maximum possible life expectancy, rather than planning around the average and pooling the risk of a longer life.
2. Those following one of the quicker-spending paths risk running out of savings before life expectancy. For instance, spending 8% of the original pension pot per year would mean running out of cash 17 years into retirement – five years ahead of average life expectancy for a man and nine years ahead of life expectancy for a woman.
3. For UK retirees choosing income drawdown, variable investment returns can result in considerable variation and uncertainty of income in retirement and of the age at which pension savings run out.

So, how can we help people manage their retirement resources?

We can't hope – certainly in the foreseeable future – to transform all consumers into fully informed and rational economic actors. Financial literacy and capability are low across much of the population. Regulators and policymakers must accept that psychological biases often affect thought-processes and decisions even when consumers possess knowledge. As research for the FCA has shown, few want to think about living beyond age 80 as the concept is too scary (despite, note, the fact that many have octogenarians in their family).<sup>10</sup>

The first response should be monitoring people's retirement behaviours, an action that the Work and Pensions Select Committee has called for. An early warning system could provide the Government with up-to-date information on pension balances, cash withdrawals, and take-up of guidance and advice and thus give regulators and policymakers a sense of the long-term outcomes that may materialise.

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9 SMF, Nigel Keohane, Katie Evans and Ben Richards, 'Golden Years? What freedom and choice will mean for UK pensioners' (2015)

10 Ignition House (for the FCA), 'Exploring consumer decision-making and behaviour in the At-Retirement landscape' (2014)

Additional policy steps could help people confront the challenge of resourcing their longer lives. First, we should think about triggering people to plan ahead for retirement – potentially through employers or through the benefit-claims process. After this, more could be done to target advice and guidance at those who are unlikely to be able to afford regulated financial advice. When people come to make decisions, we could make people think twice ahead of withdrawing very large sums from their pensions. As it stands, those wishing to capitalise their Defined Benefit incomes must go through regulated financial advice. Why not require those who are seeking to withdraw 50% or 25% of their DC pension savings to go through the Pension Wise service? At this point, the FCA's current work on a 'rule of thumb' withdrawal rates and the framing of decisions could also be important.

Finally, we should be aware that retirement decisions are unlikely in the future to be one-off but recurrent for those individuals who drawdown their retirement resources each year. The Government, therefore, could introduce a Mid-Retirement Financial Health Check to prompt people at age 75 to re-consider their financial position and plan financially for the remainder of their lives. This would have the additional benefit of addressing concerns associated with cognitive decline in older age by encouraging individuals to put in place mechanisms for the management of their resources in old age.

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The article above draws on analysis and evidence published in 'Golden Years? What freedom and choice will mean for UK pensioners', which was published by the SMF in November 2015.



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**By Rebecca Langford**  
Policy Manager  
Money Advice Service

## Understanding the financial capability of older consumers

Financial capability is about people having the right financial skills, knowledge, attitudes, and motivations so they are able to make good decisions and the most of their money. This, combined with an inclusive financial system, can help people achieve the best possible financial wellbeing.<sup>11</sup>

In this chapter, I discuss the financial capability of older people in terms of their ability to manage money well day to day, to plan for and manage life events, and to deal with financial difficulties. And what that means for the way older consumers make financial decisions.

### Managing money day to day

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For most working age people, managing money well day to day is about saving to build resilience and avoiding financial difficulty. For retired people the key financial challenge is the need to manage existing financial resources over their entire retirement. They need to balance the need to make ends meet day to day while preparing for – and managing expenditure related to – life events, especially declining health and potential care costs.

Older people generally have more positive attitudes towards money than the working age population. And people's confidence in their own ability to manage their finances and choose financial products increases with age. Yet functional numeracy and awareness of key financial terms and concepts reaches its peak at retirement age then declines steeply around age 75.<sup>12</sup> So there may be a cohort of older people who are over confident in their own ability to make financial decisions and product choices.

Connection to the financial system can be an issue, with bank/building society branch closure and digital exclusion disproportionately affecting older people's financial capability. Compared to working age people, fewer older people use the internet. Of people over 55 who do, 53% don't use it for banking and 41% don't use it for purchasing goods and services.<sup>13</sup> There is a particular need for firms to keep the needs of older customers and those who care for them in mind when they innovate.

### Planning for and managing life events

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The capabilities required to plan for life events such as retirement are very different from those needed to manage money well day to day through working life. The

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<sup>11</sup> Money Advice Service 'Financial Capability Strategy for the UK' (2105) p11

<sup>12</sup> Up to around the age of 70 with 72% of 60–69 year olds feeling very confident managing their money compared to only 51% of working age people. Money Advice Service (2015) UK Financial Capability Survey: [www.fincap.org.uk/financial-capability-survey](http://www.fincap.org.uk/financial-capability-survey)

<sup>13</sup> Ofcom (2015) Technology Tracker data tables wave 1 2015

recent introduction of greater freedom about how people manage their pension savings greatly increases the choices and complexity surrounding retirement income decisions, and the need for financial capability to make well-informed decisions.

Even the most financially capable people can struggle to understand the benefits and risks of different product choices and make informed decisions about retirement planning. Pension language and jargon make the market difficult for people to navigate and the ease with which people can access their information related to their retirement savings and options can be improved. Industry, regulators and organisations representing consumer interests must work together to do this.

As well as 'predictable' life events such as retirement, older people will encounter unpredictable life events such as ill health, cognitive decline and reduced mobility that have a significant bearing on how they manage their money. For example, traveling to a bank branch, using certain payment types and obtaining insurance can be more difficult. The Alzheimer's Society found that 76% of people with cognitive decline had experienced difficulties managing their finances.<sup>14</sup> Personal circumstances also leave many older people at particular risk of becoming a victim of fraud or financial abuse.<sup>15</sup>

Yet few people make plans for how they will cope with the financial impacts of declining health in retirement, for example by organising a lasting power of attorney or planning for the cost of long-term care. A majority of people aged 55+ do not even have 'a very rough idea of what they need to do' to plan for possible care costs.<sup>16</sup>

### Dealing with financial difficulty

Relatively few older people are over-indebted compared to the working age population (5% as against 16%). But a larger proportion of older people really struggle to make ends meet, and may do without essentials such as heating, to avoid getting in to debt. 13% live below the poverty line and it is estimated that 10% would not be able to replace a cooker if it broke down.<sup>17</sup> More can be done to empower people in this group maximise their income through accessing available benefits and shopping around to get the best deal on products and services.

### Addressing the financial capability challenge

Addressing the issues and challenges set out above will require the combined, concerted and coordinated efforts of a wide range of organisations and individuals.

In that way we can start to improve the accessibility of financial products and services, bearing in mind the financial capability needs of older people. We can encourage

<sup>14</sup> Alzheimer's Society, 'Short Changed: Protecting people with dementia from financial abuse' (2011)

<sup>15</sup> Age UK, 'Only the tip of the iceberg: fraud against older people' (2015)

<sup>16</sup> Money Advice Service, 'Financial Capability Survey' (2015)

<sup>17</sup> Department for Work and Pensions, 'Households Below Average Income 2013/14', supporting data tables. Sample of pensioners aged 65 and over in the UK. (2015)

older people to plan ahead, to challenge perceptions that 'it will never happen to me', and to raise awareness of the options available to assist older people to stay in control of their finances for longer.

And where vulnerability is identified, for example a pensioner struggling to access financial services, living in poverty, dealing with debt, coping with bereavement, or at risk of fraud, we can assist them to access services available to improve their situation.

This is the central premise of the financial capability strategy. To bring together organisations interested in improving financial capability, so we have a common understanding of the issues, what we want to achieve, and how we'll get there. Central to the success of the Strategy will be ensuring resources are deployed as effectively as possible. That means testing a range of approaches and conducting robust evaluation so we really understand what works in improving financial capability.

In that way we can start to improve financial capability and help older people make the most of their money.



**By James Lloyd**  
Director  
Strategic Society Centre

## To what extent are pension defaults the answer to protecting the disengaged?

The April 2015 'Freedom and Choice' changes to rules on taxation of Defined Contribution (DC) pension savings in the UK were historic, enabling savers aged 55 and over to withdraw as much of their DC pension saving as they wish paying only their marginal income tax rate.

The changes broke with the so-called 'annuities deal' that had formed the bedrock of UK pension policy since 1921, specifically, the obligation to turn tax-incentivised pension savings into a guaranteed (secure) retirement income.

In this way, April 2015 saw the UK's DC pensions framework switch from one of 'compulsory annuitisation' to 'voluntary annuitisation'.

In the coming years, it is reasonable to expect the outcomes of DC pension policy in the UK will resemble those found in the many other countries with voluntary annuitisation frameworks. In particular, evidence from other countries suggests the UK will experience the 'annuity puzzle', i.e. very low rates of annuity purchase among the older population widely observable in multiple countries, and the focus of academic research for a number of decades.

Importantly, policymakers in countries with voluntary annuitisation frameworks for DC pension savers generally see the results for the older population as problematic and inadequate, in particular, low retirement incomes relative to the amounts saved and tax-relief provided to savers. A key result of Freedom and Choice in the UK is likely to be reduced pension incomes among the older population over the coming decades as many individuals opt to place their money in savings accounts, or else spend it on repaying mortgages or one-off leisure activities.

In response to unnecessarily low pension incomes and poor financial decision-making by retirees, a number of countries with voluntary annuitisation frameworks have begun to explore the potential for using 'default pathways' for DC pension savers as a way of boosting guaranteed retirement incomes. These are automatic default decumulation pathways for DC pension savers who 'do nothing' at retirement, that steer them toward specific outcomes while preserving their right to use their pension pot as they wish.

For example, the Murray Inquiry into Australia's financial system highlighted a number of problems with the country's voluntary annuitisation system and recommended

default 'Comprehensive Income Products for Retirement' in order to improve levels of guaranteed income among retirees with DC pensions.<sup>18</sup>

As such, it would appear highly likely that in time, UK policymakers will also seek to explore and implement carefully designed pension default pathways for DC savers as a way of protecting the disengaged from simply leaving their money untouched, or placing it in low-interest current and savings accounts and treating it as 'rainy day' savings.

In this way, the decumulation phase of DC pensions policy in the UK would fall into line with the accumulation phase, where default pathways – in the forms of automatic enrolment into workplace pension saving – has become the norm.

As governments interested in default options for DC pension savers have found in countries such as Australia and South Africa, a number of issues and challenges are posed by seeking to use default pathways in this way among retirees.

First, what should comprise the default decumulation pathway for protecting disengaged DC pension savers at retirement? Ultimately, this question comes down to how an income should be derived from a person's DC pension pot, the extent of longevity risk pooling, the exposure to investment risk (and returns), and the amount that should be available as cash.

In grappling with this question, the UK's National Employment Savings Trust (NEST) has proposed an interesting 'core retirement income strategy' blueprint for its members comprising:<sup>19</sup>

- **An income drawdown fund** To provide a steady income that aims to protect members against inflation, as well as give them full flexibility to change their mind and withdraw some or all of their money.
- **A cash lump sum fund** To be highly liquid so it can be used by members for unexpected events without impacting their core income stream. If market conditions are good then this pot can be topped up with additional lump sums. This would be a fund from which members could move money in ad hoc lump sums into their bank account to use as they like.
- **Later life protected income** To be 'bought' gradually over time through small payments from the drawdown fund. This would remain refundable up to a certain age, at which point that money is locked in to ensure a secure income is available for the remainder of a member's life to protect against the risk of running out of money before they die.

*Source: NEST (2015)*

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<sup>18</sup> Murray D et al. 'Financial System Inquiry Interim Report', The Australian Government, the Treasury, Australia (2014)

<sup>19</sup> NEST, 'The future of retirement: A retirement income blueprint for NEST's members' (2015)

Second, how to ensure value for money for savers given the use of default options effectively removes individual-level market competition as a lever to ensure savers get a good deal? In July 2015, the South African National Treasury published draft default proposals which, when adopted, will require all retirement funds to operate a set of default policies that are in the long-term interests of members rather than of service providers. The regulations also prescribe the conditions that such default policies are required to meet.<sup>20</sup> In this way, South African policymakers are keen to use robust governance mechanisms to ensure value-for-money for savers opting for default options.

Third, to what extent should default pathways be one-size-fits-all in nature, or adjust to the individual characteristics of savers, for example, long-term health conditions that severely diminish life expectancy? This will involve complex trade-offs around competing policy objectives and 'fairness' to individuals.

These issues are likely to prove challenging for UK pension policymakers and regulators over coming decades. However, as other countries have found, pension defaults are likely to prove the answer to protecting the disengaged in the context of voluntary annuitisation for DC savers.

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<sup>20</sup> South African National Treasury, Draft Default Regulations & Explanatory Memo (2015)



**By Will Sandbrook**  
Executive director,  
Strategy and Public  
Policy  
National Employment  
Savings Trust (NEST)

## What are the barriers to retirement income adequacy in an ageing society?

The challenges of an ageing population for retirement income adequacy are well documented.

Current workers contribute towards retirement incomes both through their taxes and through their own contributions to private pension saving. Population ageing shifts the ratio between those paying into this system: working age savers/taxpayers – and those drawing down on it: the retired population. In recent decades, shifts in this ratio have been offset by the large ‘baby-boom’ generation acting as a balance. But now that generation is moving into retirement we are seeing this balance unwind as the ratio moves rapidly back towards the underlying trend: fewer people of working age funding more people in retirement.

This picture represents both macro-level challenges for society and Government and a significant personal financial planning challenge for millions of individuals in the ‘DC generation’: those whose experience of retirement saving has taken place mostly or wholly post the decline of Defined Benefit (DB) pensions and since Defined Contribution (DC) pensions became the dominant form of active provision.

The transition to DC has brought with it other shifts. Average contributions from employers have fallen, often resulting in lower participation. And there has been a shift in the dominant governance structure of pension provision away from trusts and towards retail and contract-based models. This latter shift has meant that those risks which, in any DC system, rest ultimately with individuals must be directly managed by them too.

The DC generation also has other barriers to saving. Average ages of entry to the labour market are later now than a generation ago as the number of people attending university has risen. For those more recently completing higher education, most have substantial debts. This will reduce the income available for saving through much of the early part of their working lives. And with house prices outstripping earnings growth for most of the population over a number of decades, increasing amounts of what is left are channelled towards saving for a deposit on a house or meeting relatively costly rent or mortgage commitments.

The DC generation, then, face significant challenges to building up retirement savings during their working age. And as they approach retirement, whenever or whatever that may mean for them, they must decide how to use those savings to support them through a much longer period of old age. In doing so, they will confront the significant behavioural barriers that relate to complex financial decisions, such as inertia, loss aversion and the tendency to prioritise consumption today at the expense

of consumption tomorrow, making good decisions harder to come by. And they face these decisions when already past their peak cognitive performance.

The risks of a generation passing into retirement without adequate provision are therefore considerable. While the 'baby boomers' are, for the most part, well-insulated financially against the challenges of living for longer, those immediately behind them may not be. What can be done?

Auto enrolment is a key part of the answer. The requirement to automatically enrol workers into a pension has already more than fully reversed the decline in coverage of retirement saving seen over the preceding three decades. More people are actively saving for retirement in the UK now than at any point in history.

But simply increasing coverage is not enough. For our retirement system to be truly sustainable against the challenges of an ageing population there are several other areas that must be addressed.

First, how can we encourage and enable people to save more than the default minimum of 8% of banded earnings? For many, 8% is unlikely to be enough to meet their aspirations, particularly when you take into account contribution 'breaks' during careers. So while auto enrolment at 8% is a vital start and a good news story, ways to increase contributions may nonetheless need to be found, whether through further changes in Government policy, an expanded role for employers or simply through better engagement and guidance for savers.

Second, how can we address the challenges people face in making decisions and choices about how to use their savings once in retirement? The focus since the announcement of the 'freedom and choice' agenda has been on the provision of information, advice and guidance at the point of retirement to support decisions.

These are vital components of a well-functioning retirement system. But while a good and necessary starting point, they may not be sufficient. We believe we need to consider how to engage people through their working lives so that decisions at retirement are not binary and one-off but rather a step in a longer process. We also want to ensure that when people come to make choices, the products available to them are appropriate and well-designed. And evidence suggests that whatever efforts we make, not everyone can or will engage, even if support is free and readily available. Some provision, probably leaning on default retirement paths in some way, will also be needed for this group.

Auto enrolment, coupled with the new retirement freedoms, creates a fantastic platform for the UK to respond to the challenges of societal ageing, in pensions terms at least. We are at an important turning point for the retirement system in the UK. There's an opportunity in front of us to build on this platform and create a credible and sustainable response. Whether, how and to what extent we maximise that opportunity is the challenge for policymakers, regulators and the industry in the months and years to come.

## **2. Accessing financial products and services**





**By Sue Lewis**  
On behalf of the  
Financial Services  
Consumer Panel

## How well do financial products and services meet the needs of older consumers?

The number of people in the UK aged 65 or over is projected to rise by nearly half in the next 20 years, and most of them will need financial services.<sup>21</sup> Older people want what everyone else does: to get the financial products and services they need at a fair price; and to have open and transparent dealings with providers. Yet their needs and aspirations are likely to be different from younger generations, and the problems they encounter are different, too.

Access to products and services can be a problem: older people are less likely to be digitally included – although that is changing rapidly – and prefer accessing services face to face.<sup>22</sup> This means they can struggle in a world where online services are becoming the norm, and banks are withdrawing their high street presence.

There is evidence to suggest older consumers are less financially capable, particularly when it comes to choosing products, and often slower to process information.<sup>23</sup> However, this is different to cognitive decline, which isn't likely to set in to a significant degree until age 75 or later.

Older people are likely to find themselves victims of age discrimination. This is not permitted in most service industries, but financial services are exempt.<sup>24</sup> Firms can use age as a risk factor in pricing financial products, or even refuse to provide products to certain age groups. So at an age when they have more leisure time to visit friends and family, or take a holiday, older consumers find they cannot get travel or car insurance, or that it is exorbitantly priced: 97% of annual travel insurance policies impose an upper age limit for new customers.<sup>25</sup> Premiums rise steadily with age, although this doesn't necessarily reflect the cost of serving older age groups.<sup>26</sup> The insurance industry can no longer take gender into account when setting prices,<sup>27</sup> so we question whether it should be allowed to discriminate against older people.

21 Age UK, 'Later Life in the United Kingdom' (December 2015):

[www.ageuk.org.uk/Documents/EN-GB/Factsheets/Later\\_Life\\_UK\\_factsheet.pdf?dtrk=true](http://www.ageuk.org.uk/Documents/EN-GB/Factsheets/Later_Life_UK_factsheet.pdf?dtrk=true)

22 An Age UK Digital Inclusion Policy Review document states only 29% of adults aged 75 years and over have used the internet: [www.ageuk.org.uk/PageFiles/12810/Digital%20Inclusion%20Review.pdf?dtrk=true](http://www.ageuk.org.uk/PageFiles/12810/Digital%20Inclusion%20Review.pdf?dtrk=true)

23 Age UK, 'An Inclusive Approach to Financial Products': [www.ageuk.org.uk/documents/en-gb/professionals/research/beyond%20financial%20inclusion%20\(2008\)\\_pro.pdf?dtrk=true](http://www.ageuk.org.uk/documents/en-gb/professionals/research/beyond%20financial%20inclusion%20(2008)_pro.pdf?dtrk=true)

24 Section 3 of the Equality Act 2010 (Age Exceptions) Order 2012 – financial services include a service of banking, credit, insurance, personal pension, investment or payment nature.

25 Age UK, 'Later Life in the United Kingdom' (December 2015):

[www.ageuk.org.uk/Documents/EN-GB/Factsheets/Later\\_Life\\_UK\\_factsheet.pdf?dtrk=true](http://www.ageuk.org.uk/Documents/EN-GB/Factsheets/Later_Life_UK_factsheet.pdf?dtrk=true)

26 [www.telegraph.co.uk/finance/personalfinance/insurance/10946133/Travel-insurance-costs-ramped-up-for-older-travellers-even-though-claims-fall.html](http://www.telegraph.co.uk/finance/personalfinance/insurance/10946133/Travel-insurance-costs-ramped-up-for-older-travellers-even-though-claims-fall.html)

27 C-236/09 – Association Belge des Consommateurs Test-Achats and Others

The FCA's mortgage market review has resulted in providers applying stricter affordability criteria for mortgages, with most setting a maximum age limit on mortgage deals. There is some evidence that the mortgage industry is reconsidering this, but it needs to happen faster as many people are stuck in a poor deal and unable to switch to a new provider based on a factor they are unable to change.<sup>28</sup>

Without access to traditional mortgages, older people may be forced into the alternative market of equity release. For many, their home will be their most valuable asset, yet trying to release cash from it is fraught with difficulty. While most equity release schemes are classified as mortgages, their terms and conditions are wholly different from more traditional and familiar products, with much higher charges and interest rates prevalent. Providers justify these higher charges as the only way of both making a profit and supplying features such as a 'no negative equity guarantee'. The market is neither competitive nor innovative, with three main providers and three main adviser networks pricing out smaller more innovative players.

Perhaps the biggest challenge for older people is the need to 'decumulate' assets, opening up a whole new world of complex products. Although annuities had their problems, they at least gave a guaranteed income for life.<sup>29</sup> Now, people have the option of managing their own longevity risk. Around two-thirds are choosing to cash in their pension pots. Most of these (88%) have retirement savings of less than £30,000.<sup>30</sup> Although the decision to cash in may appear straightforward, the traps are many: an unexpected tax bill, losing benefits entitlements, pressure from creditors.

Many people are taking these complex decisions without advice or guidance. Only 8% of those who took advantage of the pension freedoms did so after speaking to Pension Wise; only 58% who wanted a drawdown product used a regulated adviser; and just 37% who bought an annuity used a regulated adviser.<sup>31,32,33</sup> In over half of cases, people stayed with their existing provider, missing out on the potential benefits of shopping around. Others bought these complex products through online 'non-advice' channels, and may have done so without understanding the consumer protections they lost.

While buying online often means better prices, it is not always the case for income generating products: 'non-advised' sales can still attract commission payments, which are not transparent to the consumer. Commission was banned for advised

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28 Building Societies Association, 'Lending Into Retirement Interim Report' (November 2015): [www.bsa.org.uk/document-library/information/publications/lending-into-retirement-report.aspx](http://www.bsa.org.uk/document-library/information/publications/lending-into-retirement-report.aspx)

29 Financial Services Consumer Panel, 'Discussion Paper on Annuities' (2013): [www.fs-cp.org.uk/sites/default/files/annuities\\_position\\_paper\\_20131203.pdf](http://www.fs-cp.org.uk/sites/default/files/annuities_position_paper_20131203.pdf)

30 FCA 'Retirement Income Market Data: July – September 2015': [www.fca.org.uk/your-fca/documents/retirement-income-market-data-july-september-2015](http://www.fca.org.uk/your-fca/documents/retirement-income-market-data-july-september-2015)

31 'FT Adviser' article quoting research commissioned by Zurich (November 2015): [www.ftadviser.com/2015/11/06/pensions/personal-pensions/pension-wise-hits-back-at-zurich-take-up-claim-ftHtjXQAQUOPORUq4HD4WL/article.html](http://www.ftadviser.com/2015/11/06/pensions/personal-pensions/pension-wise-hits-back-at-zurich-take-up-claim-ftHtjXQAQUOPORUq4HD4WL/article.html)

32 FCA 'Retirement Income Market Data: July – September 2015': [www.fca.org.uk/your-fca/documents/retirement-income-market-data-july-september-2015](http://www.fca.org.uk/your-fca/documents/retirement-income-market-data-july-september-2015)

33 Ibid

sales of investment products following the retail distribution review. Allowing it for non-advised sales is an anomaly.

All things considered, the risk of another mis-selling scandal such as that we saw with personal pensions in the early 1990s – which led to £12 billion in compensation being paid out – seems high, while the long-term benefits of pension freedoms remain unclear.<sup>34</sup>

The industry should think about *how* it serves its older customers. Products designed for older people are complicated and, in many cases, there is no experience of ‘learning by doing’. It is therefore imperative that the industry explains products simply, and takes account of the particular needs of older consumers, which might include, for example, using larger font sizes, or more interactive contact through face-to-face meetings or online video chats, like Skype.

The Panel has argued the simplest – and best – way of ensuring firms meet consumers’ needs, whatever their age, is to amend the Financial Services and Markets Act to place a duty of care on firms.<sup>35</sup> Detailed FCA rules should be framed to ensure firms take into account the complexity and risk of the product they are offering, and the level of financial knowledge and understanding of the customer. It would place responsibility on firms to ensure the person they are selling to has understood the features, risks and costs of a product.

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<sup>34</sup> 11.8 billion compensation for pensions and FSAVC reviews:

[www.fsa.gov.uk/library/communication/pr/2002/070.shtml](http://www.fsa.gov.uk/library/communication/pr/2002/070.shtml)

<sup>35</sup> Consumer Panel Position Paper on Duty of Care (June 2015):

[www.fs-cp.org.uk/sites/default/files/fscp\\_position\\_paper\\_on\\_duty\\_of\\_care\\_2015.pdf](http://www.fs-cp.org.uk/sites/default/files/fscp_position_paper_on_duty_of_care_2015.pdf)



## How can firms ensure that their channels of communication adapt to meet the needs of older consumers?

**By Eric Leenders**  
Managing Director,  
Retail and Commercial  
Banking  
British Bankers'  
Association

Retail banking is undergoing rapid change, driven by evolving consumer demographics, habits and preferences, insight provided by behavioural economics, and by the widespread availability of new opportunities to engage through emerging technologies that provide a wider variety of channels for insights and communications.

With the spread of smart devices and the rise of mobile and digital banking services, it is necessary to constantly test, learn, evolve and adapt communications to respond to changing consumer behaviour and the needs of the UK population. In doing so, there is a balance to strike between providing the right needs-based support and avoiding making wholesale or stereotypical assumptions about capability, or circumstances, based on people's age.

### Digital

Consumers expect communications to be succinct and delivered to them immediately when required/at point of purchase/decision across all age groups. Our published research shows that older customers who use mobile and internet banking typically use it as frequently or only slightly less often than younger generations:<sup>36</sup>

- Nearly 2.3 million customers aged over 70 are now registered to use internet banking; more than 600,000 of these people are 80+.
- There have been over 457,000 downloads of banking apps which allow users to safely pay bills, transfer money and read account statements by customers aged 60 or over. Nearly 20,000 of these customers are 80+.
- More than 300,000 customers of UK banks aged 60+ have signed up to receive text alerts from their bank, which can help customers avoid fees when breaching borrowing limits.

While the complexity of safeguarding bank customers in a digital world presents a significant challenge, innovations on the high street are showing how the barriers currently separating communication channels might be removed securely to deliver a better experience for customers.

<sup>36</sup> This data is based on 2014 figures from a range of UK banks, compared to 2013 ONS Population estimates. Table with the corresponding percentages of the UK population using internet banking by age band: [www.bba.org.uk/news/press-releases/millions-of-silver-surfers-harness-mobile-and-internet-banking/#.Vo\\_DzvmLS9I](http://www.bba.org.uk/news/press-releases/millions-of-silver-surfers-harness-mobile-and-internet-banking/#.Vo_DzvmLS9I). The BBA's *Way We Bank Now* work: [www.bba.org.uk/landingpage/waywebanknow/](http://www.bba.org.uk/landingpage/waywebanknow/)

- Accessing mobile or internet banking via biometrics – such as fingerprint log in technology which has already been incorporated in certain banking apps – or other identification techniques, can remove the need for remembering ‘memorable words’ or multi-digit codes.
- Wristbands that use the unique electronic signals sent out by people’s hearts to confirm the customer’s identity are also being piloted.

### Transitioning empathetically

While digital will be a sought after option for many, there will be customers, particularly among the ‘oldest old’ population, who want the sense of security associated with a branch. At the same time, there are customers who simply aren’t ready for digital or cannot access the technology needed to be able to bank in this way and the industry needs to be sensitive to that.<sup>37</sup>

Banks have been reducing the size of their high-street presence; however, banking technology can complement – and improve – traditional communications and services which appeal to older customers.

- Some larger banks have harnessed video technology to allow customers to talk to staff face-to-face remotely on their smartphone, tablet or personal computer wherever Wi-Fi is available.
- Other video conferencing services being piloted allow customers to patch in friends/family or professional advisers.
- Video or graphical approaches are also increasingly being used to augment the more traditional means of disclosure and make the information and messaging clearer and simpler.
- For those who have lived without the internet, frontline bank staff in a number of Britain’s banks often act as guides who help with their first steps online.

### Vulnerability

Alongside access and financial inclusion, the industry is also actively developing its approach towards vulnerability. The BBA has launched the first ever financial services vulnerability taskforce which will provide recommendations to the industry in order to improve service for customers in vulnerable circumstances, including those within the older generation. While it would simply be wrong to assume that all elderly customers are inherently vulnerable, consumer led research has shown that older

<sup>37</sup> According to the Research Institute for Consumer Affairs (rica) and the Communications Consumer Panel’s recent research ‘Inclusive Communications’, concerns about the cost of equipment and broadband charges or a lack of confidence and skills around IT use and internet access can often act as barrier to the current elderly population to go online: [www.communicationsconsumerpanel.org.uk/research-and-reports/we-re-not-all-the-same-inclusive-communications](http://www.communicationsconsumerpanel.org.uk/research-and-reports/we-re-not-all-the-same-inclusive-communications)

people are susceptible to particular situations, such as failing eyesight, multiple disabilities and need for care, which may cause them to be vulnerable.<sup>38</sup>

- Most banks offer bank statements, personal correspondence and other documents that customers need in large or clear print, Braille or on audio tape.
- In the last year certain bank customers have been able to try out cheque imaging technologies which can prove very effective to those with physical impairment and reduce the risk of fraud which is higher for the elderly.
- Recently launched high-definition video conferencing services enable certain bank customers to complete mortgage applications in one sitting.

Communicating with vulnerable customers is not without its challenges. It is recognised that consumers are often reluctant to disclose vulnerabilities and this can make it difficult for bank staff to communicate with them in a manner which is effective to the consumer.

### **Decision making and financial advice**

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With people living and working longer, spending and retirement patterns are also changing. Following the 'pension freedoms' reforms in particular, the complexity which consumers face in their financial planning decision-making has increased substantially. Banks are currently experimenting with services that offer insights into how people manage their finances; these include reminders for paying household bills and suggestions for cheaper energy providers. The industry is also supporting the work of the Money Advice Service on financial capability, which has dedicated steering groups aiming to better raise awareness for retirement planning through communications and education.

A fresh look at the 'gap' in retail investment advice from a view of enabling banks to re-enter the advice space is important. The pensions reforms not only increase consumer need for investment advice but present a clear opportunity for greater consumer engagement by the industry. Therefore the BBA has encouraged both FAMR and Public Financial Guidance reviews to prioritise work on affordable regulated advice for investment and protection, saving into a pension and taking income in retirement for mass market customers. Utilisation of technology such as Open Data or MiData, combined with the wider availability of consumer data, facilitates the development of advice algorithms that could help older customers determine their own financial needs and suitable means for addressing these needs.<sup>39</sup>

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<sup>38</sup> According to RNIB and AgeUK's report 'Improving later life for people with sight loss', currently there are almost 2 million people aged 65 and over living with sight loss in the UK: [www.ageuk.org.uk/professional-resources-home/research/reports/health-wellbeing/improving-later-life-for-people-with-sight-loss/](http://www.ageuk.org.uk/professional-resources-home/research/reports/health-wellbeing/improving-later-life-for-people-with-sight-loss/)

<sup>39</sup> The BBA, 'World of Change' report: [www.bba.org.uk/wp-content/uploads/2015/06/World-of-change-final-online-version.pdf](http://www.bba.org.uk/wp-content/uploads/2015/06/World-of-change-final-online-version.pdf)

Financial products and services constantly evolve to cater to the demands of their target markets. An ageing UK population may very well lead to further opportunities to engage with older consumers; not everyone will want to harness new services, but it's vital that no one feels excluded from easy-to-use technology, and that banks continue to give all the support they can to those who want to learn how to join.



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**By Paul Broadhead**  
Head of  
Mortgage Policy  
Building Societies  
Association

## How can firms adapt to meet the needs of an ageing population?

Over the past couple of years the Building Societies Association (BSA) has been thinking deeply about what really good looks like in responding to the needs of an ageing population. At its heart the challenge is: how do we, as financial services firms, ensure that the needs of older customers are considered in every part of the business? Building societies are customer owned and exist for the very purpose of serving their customers' needs through every stage of their lives.

Last November we published our interim report 'Lending into Retirement' and committed to taking a range of actions. Some are simple, almost self-evident. We need to make sure that older customers are empowered with the information they need to make decisions about their finances. If you look at any major lenders' website you will find consumer guides aimed at first-time buyers. Financial services does not become less complicated as you get older, in fact with all of the recent changes to pensions, the way we live our lives and the fact that retirement is increasingly a process rather than an event it can become increasingly complex.

Secondly, firms should consider having someone at a senior management level who is a strong advocate for the needs of older customers. This 'Older Persons Champion' should think about whether every part of the business is geared to serve older customers. Are there appropriate communication channels in place? Are staff trained on how to interact with customers with differing needs in later life? Are they aware of the existence of Lasting Powers of Attorney? Are product portfolios appropriate in meeting the needs of older customers?

Perhaps naturally, much of the recent focus in the media has been on the mortgage market. The last thing we want is for credit-worthy customers to be locked out of the mortgage market on account of their age. That is why every building society has committed to review its maximum age policy.

Some age policies might stay the same, some might move up and some might go altogether. Of course, that depends on any particular lender's expertise, risk appetite, systems, processes, and knowledge of the market. But let's imagine for a second that the entire mortgage industry decided to do away with maximum age limits. What would firms in the mortgage sector look like?

Immediately we might think that this could blur the boundaries between a traditional mortgage and a lifetime mortgage. That is a fair challenge, if a mortgage term extends beyond a borrower's expected lifespan then implicitly it is expected that the capital will be recovered from the borrower's estate. With a traditional mortgage the lender, and the regulator, expects the capital to be paid back at the end of the term.

It is right that in some cases the family is consulted if possible, and legal advice is often sought in the lifetime mortgage sector for a reason. Should we legitimately

expect that the borrower should go through the same process as for the lifetime mortgage industry?

Building societies have led the way in championing lending to older borrowers to provide mortgages that are appropriate for consumers irrespective of their stage in life, but more needs to be done. We need to assess the regulatory regime alongside the demographic changes that we face to ensure it remains fit for purpose. The conversation needs to move on from what firms feel regulation may prevent. Instead regulators and industry alike should focus on the potential risks with lending to older borrowers and how firms can best mitigate them.

We often hear that a borrower in retirement with a Defined Benefit pension or one who has bought an annuity is quite a safe credit risk. They have a certain income for life – as opposed to someone of working age who might lose their job.

Although the fact is that Defined Benefit pensions are rapidly heading the way of the dodo, assessing income as people approach retirement or are in retirement will become increasingly challenging. Many borrowers are approaching retirement with less pension wealth than they anticipated.<sup>40</sup> For borrowers further away from retirement we have no guarantees they will continue to pay in, or that their investments will perform as they expect, or that they won't draw out a lump sum at the age of 55. We may also be reaching a peak of pension wealth, a trough is expected before the benefits of auto-enrolment for Defined Contribution pensions start to make an impact.

There is a need for different industries to work together to address the challenges. There could well be a role for lenders, insurers and/or pension providers to get together to design the retirement mortgages of the future, and this Discussion Paper is a great start.

It should be recognised that product innovation and regulatory change will not address all of the challenges facing society. Some small, practical changes can make a huge difference to people's lives.

Retirement is increasingly a process rather than an event; people retire from work, they do not retire from life. Older people or retirees are not a homogenous group, their needs vary as much as at any life stage. If a person is fit and well they will want access to the same suite of financial services products as anybody else. If a person is in deteriorating health, either mentally or physically, then they need to be able to access their finances in an appropriate manner without feeling that they are a burden on their family.

Our members know that people want to interact in different ways. Some people want to interact electronically; others are not so e-savvy. It would be wrong to assume that

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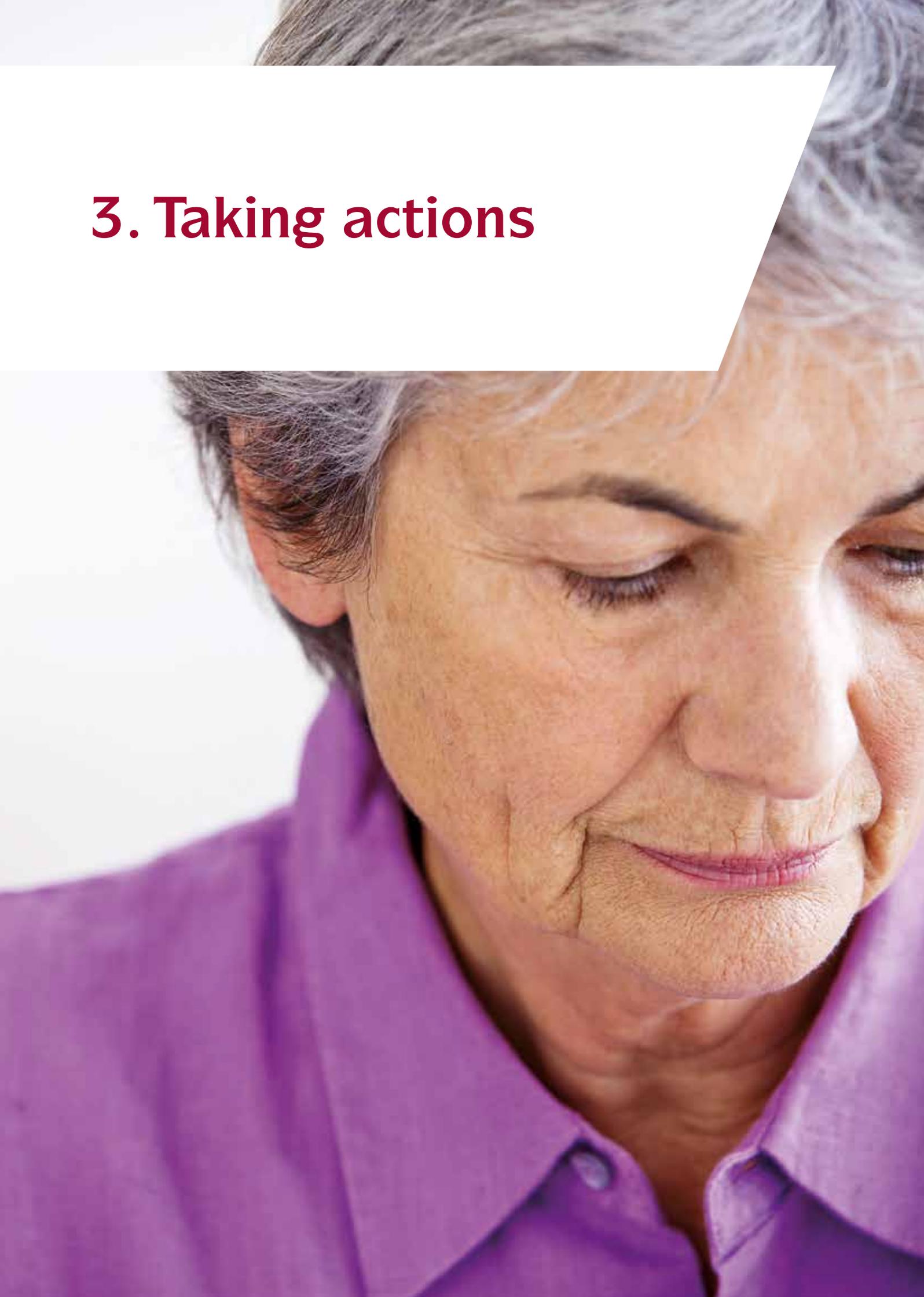
40 Aviva Real Retirement Report, 'Are you fit to retire?' (Summer 2015):  
[www.aviva.com/media/upload/18\\_07\\_15\\_RRR\\_special\\_-\\_Are\\_you\\_fit\\_cropped\\_unlocked.pdf](http://www.aviva.com/media/upload/18_07_15_RRR_special_-_Are_you_fit_cropped_unlocked.pdf)

in the future older customers will be less likely to interact using digital media, many currently do so, and as time goes on it will become the norm for many people. That said, it is also important to recognise that people do have different needs. Some of our members have been providing home visits to those that have difficulty getting out of their homes; we have one member that provides a drive-through branch, because the many of their customers are elderly, cannot walk very far, but are car drivers.

Some branches are moving to lower counters, often with stools or seats, so that customers that cannot walk very far can sit down while they are transacting because it makes it more comfortable, and they can maintain their independence.

A mix of solutions is needed to meet the challenges our changing demographic presents. We need to come together to address these challenges now before we risk certain customer segments finding difficulty accessing the financial services that they need.

# 3. Taking actions





**By Keith Richards**  
Chief Executive Officer  
Personal Finance  
Society

## What is the role of advice for our ageing population?

Whilst some comfort and confidence can be derived from the fact that we are living much longer in retirement than ever before, this also brings with it a number of financial challenges and the increasing risk of hardship through what should otherwise be the 'Golden Years'.

With the introduction of pension freedoms offering even greater control and choice over our pension funds, the need for professional advice to deliver the benefit of effective financial planning has become even more evident and valuable. An ageing population in the UK presents substantial, complex and increasing challenges not only for Government and regulators, but also the financial services industry too.

The availability of readily accessible generic information and guidance are going to be essential in supporting the public and long-term solutions will ultimately require a coherent vision about what the challenges are, where the priorities lie and how as a society we will attempt to deal with them. In turn, this will require honest and open debate about things such as the future responsibilities of the State versus the Individual, potentially leading to more sustainable public services and increasingly relevant and accessible solutions at individual consumer level. In this context, increasing access to relevant financial advice, innovative products and support services, at a price that is affordable, represents both an opportunity and a challenge. Hand-in-hand with that is the need to continue to re-establish consumer confidence in the financial services sector more broadly.

Ultimately, restoring integrity will require greater understanding by the consumer of the financial landscape and the value of advice in terms the consumer can directly relate to, supported by proportionate and balanced reporting in the media. That said, the good news is that recent research indicates that consumers over the age of 55 are more likely to be influenced positively by financial advisers and although the metric used decreases after the age of 75, it still remains positive compared to many other alternatives.<sup>41</sup> This is welcome news, given the increasing need for financial advice to help meet the substantial financial challenges typical of our ageing population, as well as those arising specifically from recent Government interventions, such as pension freedoms.

Key to this is a growing need for advice in respect of cash flow management over increasingly longer periods in retirement during which the risk of running out of money has also increased. Retirees increasingly need help with striking the right balance between flexibility and security of income; taxation and greater understanding in respect of the provision and funding of health and social care.

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<sup>41</sup> 'Planning Tomorrow Today – Financial Advice Market Review – A response from the International Longevity Centre' (Dec 2015)

Given their desire and commitment to deliver the best advice possible, underpinning these issues is a need for advisers (and policymakers) to keep up-to-date with trends in longevity and morbidity as well as typical patterns of consumption and expenditure during retirement.

Without this, it will be difficult for advisers to help ageing consumers take full advantage of the new flexibilities in ways that best meet their long-term income needs. It is perhaps partly due to these complexities and a growing, research-based understanding of them, that we have seen the development of specialist 'later life' services taking a much needed holistic, joined-up approach to financial planning. This includes cash flow forecasting, income strategies, portfolio management, the use of residential property, tax (including generational wealth transfer strategies) and legal advice.

The role of guidance services such as Pension Wise will remain important in offering generic information to help individuals along the path of long-term planning, prioritisation and the avoidance of scams. This will hopefully circumnavigate the worst outcomes for those who take it. That said, it is critical that guidance efficiently sign-posts individuals to qualified regulated financial advice when appropriate to help them maximise their financial position and provide certain protections. Unlike some other demographic segments, the older consumer typically has little time to recover financially from inappropriate or sub-optimal actions impacting negatively on their finances.

The provision of social care and its funding deserves specific mention, with about three-quarters of 65-year-olds needing care at some point in their lifetime.<sup>42</sup> However, the current care market is both confused and confusing. Consequently, a lack of clarity in respect of the distinction between health and social care and their respective funding lies at the root of most consumer disputes. There is a critical and growing need for information and guidance in respect of how the market works and how to access the appropriate care specialist financial advice when planning and preparing to pay for it.

In this respect, the Care Act 2014 makes it a statutory requirement for Local Authorities in England to provide access to comprehensive information and advice about care and support services in the local area to all residents, including access to regulated financial advice. That said, Pension Wise is well positioned to provide access to similar, albeit generic information and guidance rather than advice. Similar to local authorities, Pension Wise is also required to sign-post people to regulated financial advisers with specialist qualifications and expertise.

Mindful of this need, The Personal Finance Society launched a specialist register for qualified later life advisers (who have appropriate Long Term Care qualifications) in November 2015 to help our ageing population access the qualified advice they so clearly need and can rely on.

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<sup>42</sup> Association of British Insurers: [www.bbc.co.uk/news/business-21164964](http://www.bbc.co.uk/news/business-21164964)

The PFS also launched the UK's largest 'accredited' directory of professional financial advisers where the public can check the credentials of an existing professional adviser or source one locally with confidence.<sup>43</sup>

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<sup>43</sup> [www.thepfs.org/yourmoney/find-an-adviser/](http://www.thepfs.org/yourmoney/find-an-adviser/)



**By Liz Barker**  
Global Head of  
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**Crawford  
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## Behavioural insights into the ageing mind

Insights from the behavioural sciences can help to more deeply understand older people's behaviour and decision-making. The latest research by psychologists on the ageing mind and cognitive decision-making is finding that our thinking processes change as we age, and that some cognitive biases and heuristics are often more prevalent in older people.<sup>44</sup>

Better understanding how people's decision-making changes as they grow older is essential for optimising people's lives and serving the 'Silver Economy'. With this knowledge, financial services providers can help to ensure older people make the best financial decisions for themselves, are offered products and services tailored to the older mindset and live in an environment designed to take account of these differences in decision-making.

This contribution:

- Analyses four findings about cognitive decision-making in the older mind.
- Considers what implications these differences might have for the communications, financial products and services we design which are aimed at an older consumer, or indeed, the type of decisions we ask older people to make, and considers some of the interventions and insights from behavioural science which might be applied to optimise older people's decision-making.

### The old rely more on automatic, experienced-based 'System 1' thinking

From our 20s and early 30s onwards, our reasoning and deliberative capacity (known as fluid intelligence) declines with age, and although our knowledge and experience (known as crystallised intelligence) increases with age to compensate, eventually this also starts to decline in our 70s, leading to an eventual downward trend in decision-making ability in later years.<sup>45,46</sup> For example, two studies found evidence of a peak in financial capabilities around age 60.<sup>47</sup>

44 Psychologists such as Ellen Peters, Laura Carstensen, Mara Mather, Yiwei Chen and Joseph Mikels

45 Salthouse TA (2004) What and when of cognitive aging. *Curr Dir Psychol Sci* 13(4): 140–144

46 This peak and decline in crystallised intelligence may now figure later in life as education levels, health and nutrition improve. A 2015 study at MIT and Harvard by Joshua Hartshorne and Laura Germine found that vocabulary tests revealed a peak in crystallised intelligence in people's late 60s or even early 70s. The same study also found that peaks in measures of fluid intelligence varied – some peaked early in life whilst others did not peak until age 40. See Hartshorne, Joshua K. & Laura T. Germine (2015). 'When does cognitive functioning peak? The asynchronous rise and fall of different cognitive abilities across the lifespan', *Psychological Science*, 26(4), 433–443 and MIT News: <http://news.mit.edu/2015/brain-peaks-at-different-ages-0306>

47 Agarwal S, Driscoll JC, Gabaix X, Laibson D (2009) 'The age of reason: Financial decisions over the life cycle and implications for regulation'. *Brookings Pap Econ Act* 39(2): 51–117 and Korniotis GM, Kumar A (2010) Do older investors make better investment decisions? *Rev Econ Stat* 93(1):244–265.

Day-to-day, older people tend to rely less on fluid intelligence – reasoned, deliberative thinking and more on gut-feel, intuition, rules of thumb and shortcuts (System 1 type decision-making) – things learned through experience and which can often actually lead to equally effective decision making, but only in areas they are familiar with.<sup>48</sup>

But it's also harder for them to ignore or sift through irrelevant information and their ability to absorb and process numeric information also declines. For example, when asked which numbers represented the biggest risk of getting a disease, 1 in 10, 1 in 100 or 1 in 1000, 29% of adults aged 65–94 could not answer correctly. Reduced numeracy can mean older people are more prone to framing effects.

Implications:

- This has implications for the communications we design or decisions we ask older people to make.
- We need to design financial products and services with an awareness of these changes in our thinking. For example, firms not only need to communicate and explain services in a way that are accessible to older consumers, but their products need to be designed in such a way that are understandable to the older mind.

### Older people are more affected by choice overload

Older people tend to find it harder to navigate a proliferation of choice. As a result, they tend to prefer simple choices with minimal options and information that is succinct. An 85-year-old retired engineer in the US trying to make her healthcare choices exclaimed:

'I'm 85, do I have to go through this nonsense? I'm trying to absorb all the information, but it's ridiculous. Not just ridiculous, it's scary. If there was a single card and it was administered by Medicare, and it got the cost of drugs down – wonderful, marvellous.'<sup>49</sup>

Research supports this anecdote:

- In a 2008 study where participants were asked to make healthcare choices (for prescription drug plans, physicians, and hospitals) and everyday decisions (for cars, apartments or jams), older adults did not value choice as much as the young. They tended to prefer half the number of options to younger adults and the very old (eg 80+ year olds) tended to prefer even less choice than people in their 60s and 70s.<sup>50</sup>

48 Li, Y., Gao, J., Enkavi, A.Z., Zaval, L., Weber, E., Johnson, E. 'Sound credit scores and financial decisions despite cognitive aging' PNAS January 2015, Vol 112, No.1

49 Leland J. 73 Options for Medicare Plan Fuel Chaos, Not Prescriptions. The New York Times, May 12, 2004. May 12, 2004.

50 Reed, A.E., Mikels, J., Simon, K. 'Older Adults Prefer Less Choice than Younger Adults' Psychology and Aging. 2008 Sep; 23(3): 671–675.

- Other studies have found that the old have a greater tendency to defer decisions when faced with what they perceive as too much choice. They are also less likely to experience negative emotions afterwards, such as regret or worry about not making a purchase.<sup>51</sup>

Implications:

When presenting choice to older audiences we need to:

- Be extra careful about how many options there are; 5 options will be better received than 50 or even 8.
- Structure choice and decision-making carefully by categorising it to ensure a decision is relatively easy to make and is therefore less likely to be deferred for another day.
- Ensure information is high in cognitive ease i.e. uses plain English, with clear signposts and makes salient the key information.
- Older people in general are more sensitive to loss framing so point out what losses they may incur if they postpone their decision or try to guide them to make a choice.

### Older people are more drawn to positive emotions

Emotion generally plays a larger role in decision-making for older people. They have a greater tendency to focus on, seek out and remember positive emotional experiences and find positive information and images more salient whilst either not noticing or forgetting negative messages.<sup>52</sup>

This may mean they will be more influenced by positive frames of information than negative. There is also evidence that they are more affected by loss aversion.<sup>53</sup>

Older people's tendency to focus on the positive is thought to be related to the stage they have reached in life. Gone are the goal-striving days of their youth. Instead they

51 Chen, Y. Ma, X., Pethtel, O., "Age Differences in Trade-Off Decisions: Older Adults Prefer Choice Deferral" *Psychology and Aging*. 2011 June; 26(2): 269–273

52 Research findings supporting this are numerous. For example, in one study older adults showed far greater preference for emotional advertisements relying on positive affect than others and tended to remember them better. Older people preferred airline slogans such as '*Take flight...your loved ones await*' or '*Take flight...expand your horizons*'. Notably they also demonstrated better recall of both the slogan and airline brand when these were framed positively. See Fung H.H., Carstensen L.L. "Sending memorable messages to the old: age differences in preferences and memory for advertisements." *Journal Pers Soc Psychol*. 2003 Jul;85(1):163–78 and Turk, S., Mather, M., Carstensen, L.L., "Aging and Emotional Memory: The Forgettable Nature of Negative Images for Older Adults" *Journal of Experimental Psychology*, 2003, Vol. 132, No. 2, 310–324

53 See discussion and review in Carstensen, L.L., Mikels, J. A. and Mather, M. "Aging and the intersection of cognition, motivation and emotion" In Birren, J. & Schaie, K.W. (eds) *Handbook of the Psychology of Aging* (sixth ed), San Diego: Academic Press, pp343–362.

focus on what brings emotional satisfaction, either through meaningful relationships (such as grandchildren or friendships) or ways in which to savour life, perhaps because they perceive their life is nearer its end than its beginning.<sup>54,55</sup>

Implications:

- When designing and writing communications for older people use positive messages rather than negative, fear-based messages.
- Leverage positive emotions in imagery and language as they are more likely to get their attention and be remembered.
- Frame information in a positive way rather than negative to steer decision-making.

### **Older people are more susceptible to misinformation, myths and false claims**

Although we are all susceptible to mere exposure *effects* – when we like something simply because it feels more familiar, and illusion of truth effects – when we believe something to be true because it feels familiar, older people are more likely to be affected by these effects and are therefore more susceptible to scams, myths and false claims.

This is because older people's working memory declines meaning that when they read or hear a piece of information and are subsequently told the information is false, they may later forget this significant detail and mistakenly remember it to be true. Research illustrates this. For example:

- One study found that given two criminal reports to read, with true information printed in black and false information printed in red, older people were more likely to be influenced by the false statements in their subsequent judgements.<sup>56</sup>
- Older people may fall prey to scams when misinformation suggests their memory is at fault. For example, a con artist might say 'I told you that the repair would cost £X and you agreed to pay.' One study showed that older participants were more

<sup>54</sup> This is known as 'Socioemotional Selectivity Theory' developed by Laura Carstensen.

<sup>55</sup> These findings are also supported by neuroscience, with fMRI studies showing that ageing is associated with increased activity in the amygdala for positive information and events, combined with an increase in prefrontal cortex (PFC) activity, regions particularly associated with the regulation of emotions. See Mather, M., Canli, T., English, T., Whitfield, S., Wais, P., Ochsner, K., et al. (2002). A double-dissociation in amygdala activation to emotionally valenced stimuli in old and young people. Manuscript submitted for publication & St. Jacques, P.L., Winecoff, A., & Cabeza, R. (2011). Emotion and ageing. In P. Vuilleumier, & J. Armony (Eds). Handbook of Human Affective Neuroscience. Cambridge University Press, Cambridge, UK

<sup>56</sup> Chen, Y., Blanchard-Fields, F., 'Unwanted thought: Age differences in the correction of social judgements' Psychology and Aging, 2000, Vol. 15, No. 3, 475–482. Also see How Warnings about False Claims Become Recommendations Ian Skurnik; Carolyn Yoon; Denise C Park; Norbert Schwarz Journal of Consumer Research; Mar 2005; 31, 4; ABI/INFORM Global pg. 713

likely to be 'captured' by false memory suggestions like this than were younger participants.<sup>57</sup>

Implications:

- This knowledge helps to illustrate why and how financial scammers are likely to be successful by targeting older consumers. Therefore, we need to take stronger measures to regulate against scams and help older consumers to detect scams.
- In a world where we are bombarded with information from diverse sources, many of which can be unreliable, particularly in the media and on the internet, older people's susceptibility to false claims is cause for concern. Directing them to reliable sources of information and away from poor sources is valuable.
- When communicating with older people, we need to take particular care when discussing and debunking myths that we steer clear of restating false information. Focus on stating the truth instead, particularly in the main message.
- Don't expect older people to have pin-sharp memories of people, places and things. Make communications cognitively easy for them by reminding them of names, places and facts etc.

### Conclusion

These insights from behavioural science have important implications and applications for communications, and the design of financial products and services for older consumers. How can we best frame and present choices and financial information to older people? How can we optimise their decision-making given what we know about how their brains work?

Financial services providers need to draw on these existing – and continually developing – insights to customise communications, user experience and behavioural interventions according to age, thereby optimising any intervention and increasing its likely efficacy.

In an era where older people are set to become an increasingly significant proportion of society, with different needs and abilities, making use of such insights, knowledge and understanding from the behavioural sciences will put us in good stead.

<sup>57</sup> False Remembering in the Aged; Larry L. Jacoby and Matthew G. Rhodes, *Current Directions in Psychological Science*; Vol 15, No 2, 2006



## **4. Role of firms**



**By António Simões**  
On behalf of the FCA  
Practitioner Panel

# Adapting to the changing needs of our customers

## Demographic change

Rising to the challenge of demographic change is one of the key issues facing the industry and identifying the changing needs of customers will be one of the common factors shared by firms which adapt to survive in the longer term. The most obvious dimension of change is the emergence of an ageing society which places dependency ratios under pressure as the numbers of those in work relative to those not working decline. In this context there is a temptation to present increasing longevity as a problem for societies; however it is undoubtedly one of the greatest achievements of civilization. The challenges are manageable and innovation in financial services is key. In England a newborn baby boy can now expect to live to 79.5 years (an increase of 5.9 years over two decades) and a newborn girl can expect to live to 83.2 years (an increase of 4.1 years over two decades).<sup>58</sup>

## Working more flexibly

For most people the traditional model of working for a single organisation and retiring for a few years, or relying on the pension provision of a partner, is long gone. The new environment is driven by a number of factors which the industry is considering in the context of innovation. Living for longer will, in itself, not be the only driver for change. Individuals are expected increasingly to make provision for their own later life alongside, or in place of, collective savings vehicles. Meanwhile the decumulation phase no longer starts with the cliff edge of retirement, but is likely to involve increasingly a period of semi-retirement as people move to part-time working or shift to less demanding or more adaptable jobs while continuing to draw an income.

If individuals are to take more responsibility for their own later life provision then they must have easy access to financial information. The development of easily accessible, accurate and up-to-date information on pension provision, including both state and occupational elements, is a key site of innovation. This will require the state and private sectors to work together, and the industry is keen to see this move forward. Other countries have been working on innovation in this area for many years (such as the Swedish 'orange envelope' system) and we look forward to seeing the effects of the Belgian national pension tracking service, which will be available in 2016 for state and occupational pensions. Information on its own will not facilitate more flexible later life provision; technology is crucial, for example to make transfers easier and more accessible.

<sup>58</sup> ONS 2015

In decumulation, customers and providers face new challenges. In the UK the new pension freedoms genuinely deserve the epithet 'revolution'. The challenge for providers is to build products which provide both flexibility and security. A window of stability in which resources can be used to develop more innovative retirement income options would help to move the market forward in this area.

### **Digitalisation**

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The use of digital solutions, such as robo-advice, will be part of the new landscape. There are undoubted benefits from such solutions as customers become used to operating in a digital environment as the norm for service transactions. Benefits include improved access to advice, lower costs and potentially better value for money. For the adviser market, technology offers the prospect of lowering fixed costs and building scale. But the industry and the regulators must be mindful that some customers are unable to interact digitally with the financial services industry, and some may only want face-to-face or other personal interactions at certain moments of their lives. Assessing vulnerability and social exclusion must be factored into any solutions and the industry is already working with the third sector and others to address this. Financial education, while necessary, is not sufficient to address vulnerability, which may be caused by many factors including individual circumstances, medical and legal issues, and may be temporary for some but long term for others.

### **Intergenerational wealth transfer**

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Much of the focus of the financial services industry has recently been on those at and around the point of retirement. An important driver for innovation is the desire for customers to balance their own need for financial security against the desire to support later generations who face different challenges.

Questions to be answered by the industry include how to deal with the changing demographic profile of wealth. This includes the increase in income inequality, a feature of many other industrialised countries as well as the UK,<sup>59</sup> changes to the age profile of wealth (since the financial crisis, disposable income has fallen in real terms for all age groups except the elderly), and the impact of specific generational factors (such as student loans and the absence of access to home ownership for younger generations) on the ability to deal with financial shocks and plan for the future.<sup>60</sup>

Developments in healthcare and lifestyle mean that although people may be living longer, a substantial period of this may be in poor health, requiring the funding of long-term care. Even for those who remain in robust health into old age there will still be some medical and support costs to be considered. These factors all provide opportunities to consider how to facilitate the transfer of wealth between generations in a way that meets customer needs, which will differ substantially. Pension freedoms and equity release are probably parts of the solution, but this is a market which is

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59 Institute for Fiscal Studies, 'Income inequality in the UK', (2013)

60 OECD, 'Rising inequality: youth and poor fall further behind', (June 2014)

still relatively undeveloped (lending figures for 2014 were £1.38bn against a total estimated housing stock value of over £5trn), and assets vary greatly by geographical region.<sup>61</sup>

### **The role of the regulator**

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The issues to be considered for an ageing population are vast and complex and the key point for the FCA and other financial services regulators is where to modify the regulatory settings to balance innovation and consumer protection. Addressing the areas above, including consolidating information on retirement benefits, facilitating transfer of assets and maintaining awareness of the fluid nature of vulnerability would be a good starting point.

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<sup>61</sup> Savills, 'Valuing Britain', (January 2014)



**By Dr Yvonne Braun**  
Director, Long-Term  
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## How is the insurance and long-term savings industry adapting its products and services to meet the needs of an ageing population?

The inexorable rise of people's life expectancy is a trend to be celebrated – ultimately, immortality has been a dream of humankind for millennia. But we are only gradually catching up with what this means for our society. Nor is this an issue just for 'older people' – the ageing population affects all age cohorts, in different ways.

Long-term savings providers and insurers are at the coalface of the ageing society, providing many of the products and services people rely on for their financial security as they age, and are adapting them to adjust to this immense societal shift. In doing so, the industry works with the grain of public policy. However, while we have some of the components in place to deal with the implications of an ageing society, I argue below that we need a more visionary, holistic approach to adapt successfully.

How to fund a much longer life? It is well established that consumers will increasingly have to become more self-reliant when saving for their retirement: post 2050, it becomes typical for people reaching State Pension age to not receive a Defined Benefit pension.<sup>62</sup>

Auto-enrolment into workplace pensions is of course the Government's flagship reform to ensure people have a long-term savings vehicle that will provide a retirement income, and long-term savings providers have enrolled millions of savers. But the Department for Work & Pensions' own scenario analysis shows that even with auto-enrolment complete, 11.9 million people will still be undersaving, three quarters of them on middle to higher incomes. This highlights the critical importance of increasing pension savings, and we must collectively seize the review of auto-enrolment in 2017 to turn auto-escalation and other means of increasing pension savings beyond 8% of salary into a reality.<sup>63</sup>

At the same time, the Government's freedom and choice reforms have given unprecedented flexibility at the point of retirement. After successfully implementing the reforms, providers have now started to adapt their product and service offerings, for example through combining guaranteed income with flexibility, and branching out into 'robo-advice'.

62 DWP, 'Pensioner Income Projections', (March 2015): [www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/414399/pensioner-income-projections.pdf](http://www.gov.uk/government/uploads/system/uploads/attachment_data/file/414399/pensioner-income-projections.pdf)

63 DWP, 'Scenario analysis of future pension incomes', (August 2014): [www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/341655/Scenario\\_analysis\\_of\\_future\\_pension\\_incomes.pdf](http://www.gov.uk/government/uploads/system/uploads/attachment_data/file/341655/Scenario_analysis_of_future_pension_incomes.pdf)

However, the existing framework for guidance and advice has arguably not kept pace with these major reforms. The Financial Advice Market Review provides a golden opportunity to re-think how to enable providers to give policyholders more support than is currently possible without overstepping the advice boundary. We also need a more ambitious approach to using the public financial guidance services. Providers are already signposting to Pension Wise to help customers make the most of their new pension choices. But we would like to see all public bodies use opportunities to work with industry to signpost and nudge people towards accessing advice and guidance at critical junctures in their life.

In particular, central Government should signpost the Pensions Advisory Service at age 50 for all citizens for a conversation about their pre-retirement finances, similar to the NHS' 'mid-life MOT' of people's health. This would enable a conversation about people's financial preparedness for retirement at a point where they can still make a significant difference.

Care funding should be part of this conversation as longer lifespans can also mean care costs, be they in the home or in a residential setting. More flexible retirement income products can help manage care expenses in later life, and a number of life insurance products have now come onto the market which pay out on onset of care needs, adding to the existing option of immediate needs annuities.

Better leveraging of guidance should be coupled with a much greater use of digital services. Long-term savings providers already offer access to their products through platforms which enable users to view all their products and investments with the provider in one place. But we must work together with Government to extend this concept to give people a comprehensive view of all their assets in one place – with a 'pensions dashboard' showing consumers their overall preparation for retirement, including the state pension. This would greatly improve the position today where a quarter of people over 50 have no idea how much they have saved towards their retirement.<sup>64</sup> International examples show how such dashboards can work in a very engaging way.<sup>65</sup>

More broadly, the industry is also adjusting to its ageing customers. Whilst many older people are experienced and knowledgeable at dealing with financial services products, including 'silver surfers' happily transacting online, cognitive decline can mean that some older people are vulnerable and less able to make the most of a competitive market. To address this, the ABI and BIBA published a Vulnerable Customers Code in January 2016.

Under the Code, participating insurers and brokers will implement a suite of actions to address the concern that vulnerable customers might simply renew their home or

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64 According to research by Retirement Advantage. <http://newsroom.retirementadvantage.com/one-in-four-people-facing-retirement-dont-know-pension-pot-value/>

65 ABI, 'Retirement 2050': [www.abi.org.uk/~/\\_/media/Files/Documents/Publications/Public/2015/Pensions/Retirement%202050%20Identifying%20the%20challenges%20of%20a%20changing%20world.pdf](http://www.abi.org.uk/~/_/media/Files/Documents/Publications/Public/2015/Pensions/Retirement%202050%20Identifying%20the%20challenges%20of%20a%20changing%20world.pdf)

motor policy from one year to the next without checking they are getting the cover they need at a competitive price. For example, insurers will:

- Ensure staff are adequately trained to recognise potentially vulnerable customers at renewal, and can offer flexible options to help address needs;
- Periodically review legacy policies to identify vulnerable customers to ensure they are aware of any more suitable alternative products now available; and
- Ask potentially vulnerable customers at renewal if their current policy and renewal terms meet their needs, making clear the importance of reviewing their cover.

How to define vulnerability and how to implement the code remain decisions for individual firms.

The examples above show that progress is being made in adjusting to an ageing society. However, efforts are piecemeal and not necessarily coordinated and further far-reaching policy changes, not least on pension tax relief, are on the horizon. This is too important an issue to address one policy at a time – we would like to see a broader strategy across Government, regulators, industry and political parties that truly re-imagines the future of our ageing society.



**By June Deasy**  
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Lenders

## What kind of borrowing challenges do older customers face?

We are now in an era of much less well-defined life stages: not only are there the new 'pension freedoms' making pension pots more accessible; the very concept of a retirement age has become more fluid with consequences for mortgage lenders and their existing and future customers.

The Council of Mortgage Lenders (CML) is examining these issues with its members. We already are seeing some shapes emerge from the fog. For details, look at our commissioned independent research on consumer demand for retirement borrowing; and our accompanying CML policy report, both launched late 2015.<sup>66,67</sup>

We draw a clear differentiation between lending *into* and *in* retirement, with distinct issues affecting each.

### Lending *into* retirement

Over a third of new mortgages taken out today extend beyond the borrower's 65th birthday. Longer mortgage repayment terms drive this trend – more than half of first-time buyers today are now taking out a mortgage to be repaid over a term of longer than 25 years.

There are also existing borrowers with interest-only loans; some will remortgage; others may seek new loans that extend into retirement. Not all will be successful, given regulatory requirements for lenders to satisfy themselves about the borrower's likely future capacity to service the mortgage to the end of its term.

### Lending *in* retirement

This occurs on a much smaller scale than borrowing into retirement, in decline since 2007. The value of mortgages (excluding lifetime mortgages) taken out by borrowers aged over 65 declined to around £1 billion in 2014 – accounting for only 0.5% of total annual advances.<sup>68</sup>

As for lifetime mortgages, CML data shows that just under half of all lifetime lending is to borrowers aged between the minimum 55, up to age 69 and that traditional

66 CML 'Research on Consumer Demand for Retirement':

[www.cml.org.uk/news/press-releases/cml-releases-new-research-on-consumer-demand-for-retirement/](http://www.cml.org.uk/news/press-releases/cml-releases-new-research-on-consumer-demand-for-retirement/)

67 CML report, 'Retirement Borrowing: reality, perceptions, projections and potential': [www.cml.org.uk/documents/retirement-borrowing-report/retirement-borrowing-report.pdf](http://www.cml.org.uk/documents/retirement-borrowing-report/retirement-borrowing-report.pdf)

68 CML Regulated Mortgage Survey

mortgage products remain a more common choice. Only at ages 70 and beyond does lifetime really dominates the lending landscape.

This paper goes behind these statistics to address three key areas for retirement borrowing from the lenders' perspective: affordability issues around pension reform; advice and distribution; *and* conduct and prudential risks.

### **Pension freedoms: potential impact on affordability**

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It will be some time before the full effects of the pension reforms are known, but it is a given that the end to compulsory annuitisation has the potential for major impact on borrowing behaviour later in life. The centrality of pension income to overall financial wellbeing in later life has been overtaken by events. The CML will monitor the emerging evidence base around the interaction between pension freedoms and the mortgage market – including the ways in which pensions pots are being used for mortgage payment purposes.

In terms of the approach lenders can take in their treatment of pension income in affordability calculations in this new pension freedoms era; lenders have much to consider in terms of the treatment of pension income – which was previously seen as more predictable and reliable form of income than that from employment.

With regard to affordability calculations for those borrowing *into* retirement a (by no means exhaustive) list of issues for lenders to consider includes: current fund valuation of Defined Benefit (DB) and/or Defined Contribution (DC) schemes; retirement age; the value of the pension at retirement, taking into account inflation; consideration of loss of income on death of joint borrower; and lenders' use of and reliance on pension provider projections.

When borrowing *in* retirement, the customer is likely to be drawing from an existing pension and this will be affected since April 2015, on the customer's choice of annuitisation, drawdown or cash.

Although these new risks should be assessed as part of lenders' normal underwriting processes, lenders can only make informed judgements at the time of application and approval; and they should be able to rely on this evaluation as a defence against conduct risk.

### **Advice and distribution**

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The 'traditional' timing of when to offer (and advise on) products or services for the about-to-retire has altered and become more complex; end of term is no longer invariably 65; the role of an individual's property asset over the whole of retirement requires different forms of advice from simply paying off a mortgage. Yet planning for retirement is best done as early as possible to avoid the added complexity of late stage.

How can we best match consumer attitudes and behaviour (which often is directed at the short-term) with advice (which has to have a longer time dimension)?

At present, few advisers cover residential and lifetime mortgages and investment advice. Advice is segmented, due to different regulatory regimes, different types of advisor; and different product heritage. It would help if the transition for consumers between different segments of advice was smoother. Mortgage advice for older borrowers cannot be given in isolation but has to touch on pension income; provision for long term care; and the impacts on benefits and inheritance. For many older people making borrowing decisions, lenders with advice permissions and intermediaries are not the whole story.

In terms of specific advice qualifications, demographic challenges will increasingly require more later life advice. However, anecdotal evidence highlights concerns over the different risk profile of older borrowers and the consequent conduct risks. This will have to be addressed by the industry and regulators.

### **Retirement borrowing: associated risks for lenders**

Planning for older age now requires the careful negotiation of a range of risks and uncertainties, from personal life events over which consumers have limited control (including health and disability risks, longevity risks), to the market risks associated with financial transactions.

The regulatory framework for lending into retirement should be such that lenders do not feel apprehensive about lending to borrowers beyond retirement age, because regulatory attitudes and constraints are well and consistently understood; and the challenges for lenders in evaluating whether borrowers have – and will continue to have – the necessary income to service a loan are appreciated.

Our commissioned independent research also looks at the potential role of the state in encouraging and enabling the use of housing equity in later life to meet people's retirement borrowing needs, including state-backed guarantees which enable lenders to offer lower interest rates and relatively large payments, compared with the non-state-backed products offered in the UK; and tax incentives, where released equity in income form is not subject to income tax, as in the UK.<sup>69</sup>

### **Next steps**

As demonstrated throughout this paper, the mortgage industry cannot provide solutions alone. We welcome the opportunity to work with the industry, regulators, Government and consumer representatives to address the challenges and opportunities presented by the demand for lending into and in retirement.

<sup>69</sup> CML, Consumer Demand for Retirement Borrowing, November 2015: <http://www.cml.org.uk/documents/research-report-on-consumer-demand-for-retirement-borrowing/research-report-on-consumer-demand-for-retirement-borrowing.pdf>



**By Sarah Luheshi**  
Deputy Director  
Pensions Policy  
Institute

## What would an effective financial services market look like for Defined Contribution savers?

The combination of automatic enrolment and the decline of private sector Defined Benefits (DB) have introduced an influx of Defined Contribution (DC) savers with different characteristics than those that came before. In future, a greater proportion of UK people will reach retirement with DC savings, though the average education and income level of these people will be lower than it was for DC savers pre-automatic enrolment.

Future savers are less likely to have DB savings or other non-pension savings to fall back on in the event they run out of DC savings. However, many savers are likely to reach retirement with a pot substantial enough to mean that the decisions they make about access could have a serious impact on their standard of living, while also being too low to provide sufficient income to fully support an entire retirement.

It is a key time for government, industry and other stakeholders to look at ways of making sure that the pension system is easy to navigate for all DC savers, especially those with low levels of financial capability, and that appropriate and accessible products, advice and guidance are offered.

### The DC landscape is changing

The proportion of workers saving in pensions in the private sector is increasing. Automatic enrolment has accelerated the growth of DC pension membership within the private sector, as most private sector DB schemes are now closed to new members and future accruals.<sup>70</sup>

A further change revolutionising the DC landscape is freedom and choice a policy that lifted the requirement to purchase a secure retirement income product and allows unlimited withdrawals from age 55.<sup>71</sup>

### DC decisions are complex

Decisions which individuals make in regards to accessing their DC pensions are particularly difficult. They require understanding of complex concepts such as inflation, investment and longevity risk. Levels of numeracy and financial capability are low among the UK adult population and a large number of people will require support and assistance with making decisions. Pensions Policy Institute workshop

<sup>70</sup> The Purple Book, 2015: <http://www.pensionprotectionfund.org.uk/Pages/ThePurpleBook.aspx>

<sup>71</sup> [www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/294795/freedom\\_and\\_choice\\_in\\_pensions\\_web\\_210314.pdf](http://www.gov.uk/government/uploads/system/uploads/attachment_data/file/294795/freedom_and_choice_in_pensions_web_210314.pdf)

participants ranked accessing DC savings as the most difficult lifetime step on which to make an informed decision.<sup>72</sup>

The main individual risk (above people not saving enough for retirement) is that those accessing DC savings might make poor decisions, due to a lack of understanding. This could lead to suboptimal outcomes such as running out of money or living on a lower level of income than necessary.

More DC savers with increased flexibility inevitably means that the way in which people access and use DC savings in retirement will continue to change. Currently, there is industry and stakeholder interest in the introduction of a soft (voluntary) default that includes both drawdown and a form of longevity insurance (e.g., a deferred annuity). How popular such defaults might be to consumers is unproven, nor whether they would make financial sense for someone with a median sized DC pot of around £15,000.

### Guidance and advice will need to support the most vulnerable DC savers

Decisions about accessing DC savings are likely to be very difficult for many people to make without assistance. The introduction of freedom and choice was accompanied by a new guidance and information scheme, 'Pension Wise'. The Pensions Advisory Service completed 6,850 Pension Wise telephone appointments between April and August 2015 and Citizens Advice completed 12,241 face-to-face appointments over the same period. This suggests that fewer than one in ten people accessing their pots had a Pension Wise session.<sup>73</sup> At the other end of the spectrum is regulated financial advice, where the upfront cost can make it appear less attractive or accessible to some people.

The outcome of the Financial Advice Market and Public Finance Guidance Reviews will hopefully address some of the existing guidance and advice gaps.<sup>74,75</sup>

### The industry needs to listen to the saver

There are some specific features that policymakers, regulators and the pensions industry should work together to address, specifically around:

- A reluctance or inability to plan beyond the next few years. Locking into a specific course of action either before or at retirement is generally unpopular with savers.

<sup>72</sup> Pensions Policy Institute, 'Transitions to Retirement – Supporting DC members with defaults and choices up to, into, and through retirement' (2015)

<sup>73</sup> [www.publications.parliament.uk/pa/cm201516/cmselect/cmworpen/371/37105.html#\\_idTextAnchor017](http://www.publications.parliament.uk/pa/cm201516/cmselect/cmworpen/371/37105.html#_idTextAnchor017)

<sup>74</sup> [www.gov.uk/government/publications/financial-advice-market-review-terms-of-reference](http://www.gov.uk/government/publications/financial-advice-market-review-terms-of-reference)

<sup>75</sup> <https://www.gov.uk/government/consultations/consultation-public-financial-guidance>

- A poor understanding of spending needs throughout retirement, likely life expectancy and the probability of living beyond older ages. Some savers underestimate the importance of having some form of longevity insurance.
- A lack of engagement (even very close to, or into, retirement) and a willingness to accept a provider default or invest where one is offered.
- There appears to be a degree of commonality around the appetite for investment risk and growth in pension savings post retirement and a willingness to sacrifice an element of capital protection and ease of access.
- Defaults and alternatives will need to be clearly communicated in terms of their risk and objectives.
- Savers are reluctant to make upfront commitments about locking into a certain course of action, or to hand over significant sums of capital in the early years of retirement. While these may act as barriers to the take up of some forms of annuities, concepts like longevity insurance and the payment of ongoing premiums do resonate.

If there is one overriding conclusion, it is that consumers need better help from those operating in the pensions arena. Consumers need help in understanding what they can do to make best use of DC pensions and how to do it. Or it needs to happen on their behalf. As all stakeholders, across industry and Government, work together to address gaps in guidance and advice and develop new products and default strategies, they will need to be aware that as the market changes and fluctuates, so will the support needed by consumers.



## **5. Wider landscape**



**By Jane Vass OBE**  
Head of Policy  
Age UK

## What is the impact of health on older people's interactions with financial services, and how can the situation be improved?

### The diversity of older people

Older people are above all diverse. In talking about health and financial services, it is important not to create the impression that everyone develops limiting health conditions as they grow older. Many people remain fit, well and cognitively alert right to the end of their lives. Most older people report high states of wellbeing and are resilient to the ups and downs of life.<sup>76</sup> These positive observations are important, because financial service providers are frequently concerned about risk, but the risks associated with ageing should not be exaggerated. They are tractable and manageable.

### Life expectancy and disability free life expectancy (DFLE)

Having said this, there *are* health conditions that develop in later life that may affect the interaction between consumers and financial services providers. From age 65, men and women can expect to live an average of 11 years without disability. Men have a further eight years of average life expectancy (to age 84) with at least one disability and women can expect on average to live a further 11 years (to age 86) with at least one disability.<sup>77</sup> There is a high degree of variation. In different parts of the country the average disability free life expectancy varies from six years to 15 years, depending on gender and socio-economic setting.<sup>78</sup> The incidence of multiple difficulties with activities of daily living increases gradually with age. One fifth of people in their late eighties have five or more such difficulties.<sup>79</sup>

### The impact of disability on access to financial services

Difficulties of daily living do not reduce the need for banking and financial services, but do present design and service challenges to the financial sector. One correspondent to Age UK described his banking difficulties in the following terms:

76 Deary I, 'Cognitive and mental health' in 'Improving Later Life – Vulnerability and resilience in older people', Age UK, (2015), p 62

77 Mortimer J and Green M, The Health and Care of Older People in England 2015, Age UK, (October 2015), pp 11–12

78 Sub-national health expectancies, Disability-Free Life Expectancy by Upper Tier Local Authority: England, (2009–11), ONS

79 English Longitudinal Study of Ageing (2014) cited in Mortimer & Green, (2015), p 15

'It is winter, the only wheelchair accessible branch is seven miles away and the infrequent bus would mean a two to three hour round trip. Internet banking requires adequate speeds, reliable connections, adequate security and skill, none of which I can guarantee. My county's rural broadband scheme is significantly delayed and will not directly benefit this property. Phone is superficially promising but like the other options, it is a lengthy process requiring a lot to be taken in on the spot and requires having a lot of information to hand or memorised... I only have restricted use of one hand (the 'wrong' one) – so it is hard to listen, write and key or handle papers while on the phone.'

One participant in an Age UK workshop on 'age friendly banking' described a particular ATM in her town that she could not get her card out of, because of arthritis in her hands – the machine did not liberate enough plastic for her to get a grip. Age-friendly design – of ATMs, bankcards, branches and other facilities – should be built in as the default.

### Challenges of cognitive decline

Cognitive decline among older customers can be a challenge for financial service providers, but again the risk should be properly assessed and not over-estimated. The prevalence of dementia only reaches 5% at the age of 80, before rising to peaks of 20% for men and 30% for women aged 95–99.<sup>80</sup> The great majority of older people remain dementia-free their whole lives.

For those who do lose mental capacity, Powers of Attorney and Court of Protection Deputyships are the established methods of managing financial affairs (processes differ slightly in Scotland and Northern Ireland). Care must be taken that the degree of delegation matches the preferences of the customer. For normal age-related cognitive change or mild cognitive impairment, financial services providers need to make sure their systems and staff are attuned to recognise the situation and make appropriate service adjustments.

### Banking assistance from unpaid carers

Another challenge arises from the caring relationship. There are over nine million unpaid carers in the UK, many of whom assist the people they are caring for in some aspect of the financial affairs, for example withdrawing cash, paying bills or buying shopping.<sup>81</sup> Quite often this is managed informally by means of lending a debit card along with its PIN number, creating a security risk and breaching the terms and conditions of use. Banks have begun to realise they need a more sophisticated suite of solutions for carer banking, to fill the space between the debit card and a Lasting Power of Attorney.

<sup>80</sup> Age UK and University of Exeter Medical School, (2015), cited in Mortimer & Green (2015), p 20.

<sup>81</sup> ONS UK population estimates by age, (2014): Mortimer & Green 2015, p 30

In parallel with assisting carers and attorneys, banks and other financial services providers have to be alert to the possibility of fraud and abuse, training staff and developing systems to detect criminal behaviour and intercept financial theft in live time wherever possible.

### **Dealing with crises**

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Health crises often create financial crises, at moments when people are least able to cope with them. Accidents, illness, bereavement, going into residential care – all can create severe financial stress. Financial services providers can assist in these situations by having processes that make them aware of what is going on for their customers and making appropriate adjustments, including to loan repayment schedules.

### **Loneliness and loss of mental wellbeing**

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Many people in later life may experience loneliness, through the loss of a spouse, death of friends, reduction in social activity or physical limitations on getting out. Poor mental wellbeing can affect people's interaction with financial services, as it increases difficulties with activities of daily living and places people at greater risk of scams and abuse.<sup>82</sup>

Banks and other financial services providers can respond by developing techniques of identifying and reacting appropriately to the needs of customers experiencing greater vulnerability.

### **Older people as healthy customers**

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Talking about health in later life can seem to carry a negative message, but, as emphasised at the beginning of this article, it is important to remember that most older people are healthy and resilient, active customers of the financial services industry, and often users of new technology. Older people are a growing proportion of the population and therefore a growing customer base for the financial services sector, which increasingly realises that it needs to adapt its approaches and services accordingly.<sup>83</sup>

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<sup>82</sup> Gale C, 'Cognitive and mental health: Mental wellbeing' in 'Improving later life – Vulnerability and resilience in older people', Age UK, (2015), p 74.

<sup>83</sup> Those aged 60+ are forecast to be 30% of the population in 2037 (ONS Population Projections).



**By Richard Lloyd**  
Executive Director  
Which?

## How have the pensions reforms affected the recently retired, and are products and services adapting sufficiently to meet consumer needs?

The recent pension reforms have given people approaching retirement much greater flexibility and choice in how to access their pension savings. Before April 2015, most people had no choice but to buy an annuity, which provided a guaranteed income in retirement. However, low interest rates, concerns over mis-selling and a lack of shopping around meant that some people who had saved into their pension all through their working life ended up getting a poor deal, and recent Which? research shows that half of people (49%) say they are worried about the value of their pension.<sup>84</sup>

By effectively removing the need to buy an annuity, the Government has given people more freedom to decide how and when they access their money, and many have taken the opportunity to withdraw their savings more flexibly. Many have opted to take cash lump sum payments from their pension pots, and retirees are increasingly rejecting annuities in favour of alternative retirement income products, such as income drawdown, that were previously only available to those with more substantial pension savings.

While giving people more choice is a good thing, turning pension savings into a retirement income is one of the most complex financial decisions many people will have to make, and one that most cannot afford to get wrong. It is therefore more critical than ever that the market works well for consumers. In essence, people should be able to achieve good value for money from retirement products that suit their needs, be protected against scams and get good quality advice in its broadest sense. However, nine months since the reforms were introduced, there remains much to be done.

First, in a market that is characterised by low levels of consumer engagement, people approaching retirement need to receive all the right information about their pensions at the right time, and have access to good quality guidance and advice in order to make good decisions about what to do next. The Financial Advice Market Review and consultation on public financial guidance will hopefully tackle some of these issues and come up with useful recommendations to meet consumers' needs, but this will mean little to those who have already made irreversible retirement decisions.

<sup>84</sup> Populus, on behalf of Which?, conducted an online survey of 2,090 adults on 2 and 3 December 2015. Data were weighted to be representative of all UK adults.

Many suggestions have been made to improve and extend Pension Wise so that it provides a better, more personalised service, while support continues to grow for a 'pensions dashboard', which would enable people to see all their pensions and savings in one place. Driven by Government, but developed and implemented by industry, this could go a long way to providing everyone with the information they need to properly engage with their pension savings, and should be given the priority it deserves.

Secondly, people need to be confident that the products they are choosing offer good value for money and suit their needs. The pensions market has not had the best reputation for treating consumers fairly in the past, and Which? research found only one in four people (26%) trust long-term financial products such as pensions to act in their best interest.<sup>85</sup> Pension providers have encountered a number of teething problems when implementing the new reforms. Recent retirees have suffered from delays and complications when trying to access their pension; a number of companies have decided not to offer all the flexibilities, while others are still developing new products and have provided conflicting information to customers. Some customers have had to wait weeks to discuss their options, been faced with high exit penalties, and experienced inconsistencies in the way the risks of pension freedom have been explained.

Since April 2015, many retirees have chosen to invest their pension in income drawdown products rather than buy an annuity. However, it is extremely difficult to compare and find the cheapest product, as there are wide variations in how providers charge multiple types of fees, and the high level of some products' charges means that they are unlikely to offer value for money, and are therefore likely to be unsuitable for most people.<sup>86</sup> We must learn lessons from the problems of the annuity market. With such big differences in cost, and confusing charges that make it difficult to compare, more needs to be done to make sure income drawdown products do not result in equally poor outcomes.

Consideration must also be given to likely consumer behaviour. ABI figures show that in the first six months of the reforms, 40% of people buying an income drawdown policy did not change provider, and 60% of those buying an annuity did so from their existing provider.<sup>87</sup> As is the case during the pension accumulation phase, consumers who do not or cannot navigate the complex pension landscape will need added protection to ensure they receive value for money. There is a strong case for retirees who do not make an active choice to be prevented from being defaulted into poor value schemes with their existing provider.

Aside from high charges, we need to assess how well alternative retirement income products are adapting to meet pensioners' different, and changing, needs. Contrary to some predictions, the pension reforms did not sound the death knell for the

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<sup>85</sup> *ibid*

<sup>86</sup> [www.which.co.uk/news/2015/07/the-true-cost-of-pension-freedom-409249/](http://www.which.co.uk/news/2015/07/the-true-cost-of-pension-freedom-409249/)

<sup>87</sup> [www.abi.org.uk/News/News-releases/2015/11/Pension-Stats-six-months-on](http://www.abi.org.uk/News/News-releases/2015/11/Pension-Stats-six-months-on)

annuity, and increasing life-expectancy rates, combined with consumers' tendency to under estimate longevity, indicates that there is still an important role for a product that offers a guaranteed income in later life. There is demand, therefore, for deferred annuities and different models that offer flexible access in the early stages of retirement alongside a guaranteed income later in life to protect against longevity risk. However, innovation to date has been fairly limited, and a close eye must be kept on any hybrid products to ensure that they offer good value and good outcomes for consumers.

Finally, the creation of a secondary annuity market will give pensioners the chance to sell their guaranteed future income for a cash lump sum. For most people, this will not be the best decision, but it will be no doubt be attractive to those who want more flexibility and feel they were forced into buying an unsuitable annuity in the past. What is clear is that these people must be properly protected. As with the wider pension reforms, there is a significant challenge to balance the freedoms with necessary safeguards, to ensure everyone can make the most of their new pension freedoms.



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**By Lesley Titcomb**  
Chief Executive  
the Pensions Regulator

## The role of the employer in helping employees nearing retirement

Employer engagement has always been at the heart of the UK pension system. The concept of Defined Benefit (DB) pension schemes relies on the relationship between the scheme and its sponsor, and automatic enrolment is centred on employer duties in the workplace. But we know from our annual 'Purple Book' analysis, published jointly with the Pension Protection Fund, that employers are more aware than ever of the market risks and longevity trends associated with providing traditional DB pension schemes – and what this means for their balance sheets.

This is borne out in the numbers – 86% of employers are using Defined Contribution (DC) schemes to fulfil their automatic enrolment duties, a trend that will be even more profound as small and micro employers undergo the process. Many will be using multi-employer schemes, and will not be involved in day-to-day scheme management. While DB schemes will be paying out benefits for many decades to come, the relationship between the employer and the scheme will become more distant, with few current employees being members

Meanwhile, the Government consulted last year on potential changes to the pensions tax relief system. Tax relief is a significant incentive for employers to provide pensions and for the staff whose contributions are effectively 'topped up' via relief. Hence the Government will need to consider what impact the different options would have on incentives for employers and employees to engage with pensions.

Against this background, how can we ensure that we maintain employer engagement sufficiently to support employee retirement planning and decision making?

Members of UK pension schemes have been given greater flexibility over their own pension pots. People now have a much wider range of choices when it comes to their retirement options. Employers and trustees of pension schemes have an important role to play in enabling individuals to make informed decisions. But as UK pensions policy moves further down the road towards individual rather than collective provision, it seems like a good time to think about what employer engagement means in the 21st century.

A recent survey from the National Skills Academy for Financial Services (NSAFS) shows that 73% of employers feel that educating staff about pensions is an essential part of the support they provide to employees. While confirming the traditional, paternalistic role some employers play in providing pensions for their employees, we should ask ourselves whether this model works in a world where pension schemes may have more than one sponsoring employer or perhaps no sponsoring employers at all? Does employer engagement have to mean sponsorship?

Other countries may have answered this question already. We know from the discussions about 'defined ambition' that the previous Coalition Government was attracted by the idea of Dutch industry-wide, collective pension schemes. That particular debate focused on funding and risk-sharing, but the Dutch system also caters for different types of employer engagement like collective bargaining.

Can this work for the UK? We know that UK employers are already attracted to the idea of multi-employer schemes through our automatic enrolment experience. 'Master trusts' are a popular choice for employers, especially those with limited or no previous pension experience. As we move further down the freedom and choice agenda, I suspect that pension communications will be one of the most important ways that employers engage with their staff about both the benefits of working for them as an organisation, and making adequate provision for later life. The availability of greater freedom and choice from age 55 raises interesting and unanswered questions for employers and may increase the trend towards the notion of 'retirement' being less of a 'cliff edge' and more of a continuum. Individuals taking lump sums or drawing down their pension may want to take career breaks, or move to part-time working. Equally, some staff may feel that the greater freedom they have over their lifestyle affords them the energy and impetus to try something different or work longer than they had previously envisaged.

Our research shows that standards of member communications, and other desirable quality features, tend to be higher in large single-employer and multi-employer DC schemes. We have discouraged smaller employers in particular from setting up new small-scale trust-based schemes for automatic enrolment. Using a good quality, well-resourced master trust could be one way for employers to educate their staff about pensions and the options they have as they decide whether to 'retire' in the traditional sense, gear down or move towards a more flexible working pattern.

There may be other benefits as well. For larger employers, using master trusts can reduce costs and free up valuable time and resources which, arguably, might be better spent improving productivity. This may be one reason why EIOPA's Chairman Gabriel Bernardino has expressed an interest in designing a 'simple and transparent EU framework for Defined Contribution occupational pensions' which can harness the power of large-scale, low-cost, cross-border arrangements. We need to start thinking now about what this might mean for employer engagement.

We are at a crossroads in the UK. With the shift away from DB pensions and with a potential shift in pensions tax relief on the horizon, it may be tempting to conclude that the era of the engaged employer providing pensions for paternalistic reasons is over. However, I believe that it would be premature to do so. Automatic enrolment is helping to build a new savings culture through the workplace. Whilst the freedom and choice agenda has the potential to transform the behaviour of individuals, and also employers, in ways we cannot yet fully predict, it may also lead to new and innovative ways for employers to engage with their employees.

# Annex 1

## Questions for discussion

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We are asking you to comment to help us prioritise areas for further work. So, specifically, we would invite you to answer the following:

- **Q1:** Do you have any views on the ideas set out in this Discussion Paper and can you suggest areas of focus that would improve financial markets for older consumers?
- **Q2:** Are there specific products, services or distribution channels that are particularly associated with poor outcomes for older people?
- **Q3:** What is the role of industry and other stakeholders (collectively as a market or at an individual firm level) in addressing the issues identified?
- **Q4:** Do you have any evidence of effective approaches to meeting the needs of older people that you have already developed and tested, or that you have observed in other markets (UK and international)?
- **Q5:** Do you have any evidence of regulatory barriers that prevent effective markets for older people?

We are particularly interested in comments on markets that have not been widely covered by the contributions to this Discussion Paper.

We also welcome informal responses to this Discussion Paper, via email or through bilateral meetings. Contact us: [dp16-01@fca.org.uk](mailto:dp16-01@fca.org.uk)

We are asking for comments on this Discussion Paper by Friday 15 April 2016.

You can also send them to us using the form on our website at:  
[www.the-fca.org.uk/dp16-1-response-form](http://www.the-fca.org.uk/dp16-1-response-form)



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