Telephone: 020 7066 9346
Email: enquiries@fs-cp.org.uk

Early access to pensions savings
Pensions & Pensioners Team
Room 2/S1
HM Treasury
1 Horse Guards Road
London
SW1A 2HQ

25 February 2011

Our ref: Early access to pensions

Dear Sirs

Early Access to Pensions Savings

This is the Financial Services Consumer Panel's response to the HM Treasury consultation paper: Early access to pensions savings.

Overview

As the consultation paper makes clear, there is a wealth of conflicting research evidence available about the ideas put forward in the paper. This in itself suggests to us that the complexity of the issues is such that many consumers are simply not in a position to take a view on what changes, if any, would ultimately be most helpful to them.

There are a number of reasons why consumers do not save for their retirement and, again, the paper refers to several research reports. These reasons range from not being able to afford to save, to having to meet more immediate financial needs or perhaps for some it might be the negative impact of high charges, poor fund performance and mis-selling scandals. The proposals in the paper are clearly not designed to address these latter issues (although we believe that the FSA's Retail Distribution Review is a leap forward in dealing with commission bias and levels of professionalism), but otherwise they seem likely to remain whether the Government takes forward any of the options in the paper or not. Given this background and the lack of conclusive research evidence, we do not believe that a strong case can be made for early access to pensions savings on the basis that it would be likely to increase pensions savings.

The paper presents possible models for enabling early access to pensions savings and in particular suggests that there could be a case for allowing access to funds in order to meet pressing financial obligations on the part of the saver, or a member of the saver's family. Again, the conflicting evidence leaves us doubtful that there would be a demand for this. Using the example of an individual in arrears with mortgage payments and facing repossession, there is some logic in using the individual's own money (in the form of pensions savings) to address the immediate financial problem. We are not sure that this is feasible in practice however. It seems

unlikely that a large number of people facing repossession would have significant pensions savings in any case – and there is some evidence in the paper to support that. In addition, it also seems unlikely that the individual would then go on to 'repay' their pension pot, creating yet another possible financial crisis in later life at a time when they would be less likely to have the ability to repair their financial position. We are concerned too that if pension savings effectively become assets that can be converted to cash at any point, there will be a demand for them to be available as chargeable security for debt, which could be lost completely in the event of bankruptcy.

While the Panel strongly supports the principle of consumer choice, on balance we believe that the solution to many of the questions around fostering a culture of saving lies not with changing the already complex pensions savings structure, but with the development of affordable linked savings and pension vehicles that provide a range of flexible savings options built mainly around consumer lifestyle and key events. In addition to the flexibility that would be offered there would have to be tax incentives similar to the pensions savings or ISA tax breaks that already exist. Consequently we see some potential in the feeder-fund model and we would be interested in seeing these ideas developed further.

Finally, if it is decided to pursue further any of the options presented in the paper or in our response, there will be a pressing need for a comprehensive information and education strategy to ensure that potential and current pensions savers are aware of the options available to them. There is a case for requiring mandatory advice for individuals who wish to access their pension savings early. Most importantly, advisers will need to be in a position to give suitable advice in this new area from the outset. We would like to see specific CPD requirements or even a specific tailored qualification put in place to address this.

Specific questions

Q1. Is early access likely to have a net positive effect on retirement outcomes for individuals?

The Panel has no new research to contribute to the debate. As is acknowledged in the paper, evidence is mixed and at times conflicting – but the percentage of respondents who indicated to the ABI[1] that an option to access part of their pension early would encourage them to save more is far outweighed by the percentage who thought that pensions were a good way of saving because they could not be accessed until retirement. One of the main reasons pensions savings has such significant tax benefits is to encourage people to save for their retirement in order to generate an income that will meet their likely needs and aspirations at that time. There is an argument to be made for greater flexibility - although there is already some flexibility within the pensions regime – to accommodate changing patterns of retirement, but there is no persuasive evidence that early access in itself is likely to lead to increased levels of pensions savings and a net positive effect on retirement outcomes for individuals.

[1] ABI quarterly survey, Q2 2010

Q2. Would early access have particular benefits or risks for traditional groups who undersave, including those on low incomes?

We suggest that, generally, individuals on low incomes do not save because they cannot afford to do so. Those on low incomes have to prioritise spending and meeting immediate and critical needs has to come first. Individuals who have debts such as credit card debts will be better off overall by repaying debt first before considering saving for retirement. The point is made in the paper that women in particular could benefit from early access to smooth their incomes across their lives. We are not persuaded that early access to *pensions* saving is the answer, but rather as we have already mentioned a flexible linked savings/pensions vehicle which incentivises saving with suitable tax breaks and allows for lifestyle changes without penalty or unnecessary complications.

Q3. Would allowing early access to pension savings in situations of acute hardship, for example where individuals face repossession of their home, help a significant proportion of people in such circumstances?

There is evidence in the paper that it would not – individuals or households with no liquid savings to fall back on in the event of hardship are also more likely to have limited or no pension savings[2]. For those that do have pensions savings and could use those funds to meet a critical financial need such as mortgage arrears, it seems unlikely that they would then be in a position to 'pay back' their pensions savings, creating further potential financial hardship in later life. Again, a flexible savings/pension vehicle could encourage those who can afford to save to set aside money for difficult times and access it if needed, but there is no reason to link this specifically to pensions savings. We also have some concerns around the possibility of pensions savings becoming chargeable assets that could be taken by creditors in the event of severe financial difficulty or bankruptcy.

Q4. Is there an argument for early access as a way of promoting intergenerational redistribution of pensions wealth in cases where a pension saver's relatives face specific financial difficulties?

The Panel has no additional evidence to support the argument one way or another. At the human level there is no doubt that, for example, parents would wish to do what they could to help their children in cases of financial need, but at a cost to their own welfare in retirement. This suggests to us simply shifting the potential burden on the public purse from the needs of the children now to the needs of the parents later and is not, therefore, a solution.

Q5. Would this create more risks for an individual's income in retirement?

Yes, almost inevitably.

Q6. What are the relative merits of the early access models outlined in Chapter 3, or any alterative options the Government should consider?

[2] Social Market Foundation Early Access to Pension Savings (March 2010)

The Panel has no additional evidence to offer on the merits of the early access models in the paper, nor suggestions for additional models for accessing pensions savings that the Government could consider. As regards the loan model, aside from the complexity of the arrangement we do not see how this would work in practice. What would happen if an individual became indebted to him/herself by failing to meet interest and capital requirements? Permanent withdrawal or other early access still leaves the issue of reduced income in later life. As we have suggested, we can see a clearer argument for developing flexible savings/pensions products possibly on the lines of the feeder-fund arrangement, although the Panel is not in a position to design such a model itself. Such a 'lifetime savings plan' seems far more sensible and feasible than focusing only on access to pensions savings.

Q7. What evidence is there of the likely impact on individuals' participation and level of pension saving, and broader outcomes in retirement of any given option?

We have no additional evidence to submit.

Q8. What would the key costs and potential burdens be of providing any of these early access options on individuals, pension providers or schemes (including if limited to cases of hardship)?

We are not in a position to comment specifically on the cost in terms of tax, National Insurance and costs to scheme administrators and providers, but clearly there will be a need for financial advisers to be fully aware of the detail and implications of any early access options and be ready to provide suitable advice. There is inevitably a cost factor and that would in all likelihood be passed on to the consumer. It may be that the issues are so complex that advice should be mandatory – again, further cost to the consumer. There will also be a need for a comprehensive programme of information for consumers, which would have to be funded by Government.

Q9. Could early access be offered by defined benefit schemes, and what would the main barriers or implications be for schemes, employers, and members?

We have no further comments to add to those already identified in the paper.

Q10. What are the potential implications for consumer advice and ensuring individuals understand the tradeoffs around early access?

We have already referred to the need for a programme of information for consumers and professional standards for advisers. Both need to understand the implications of early access to pensions savings and that will be challenging given the complexity of the pensions savings structure and the financial factors that have to be taken into consideration – for example, what will be the impact of early use of pensions saving on subsequent access to State benefits in retirement? Would tax relief be clawed back if pensions savings were accessed early? Care would also have to be taken to ensure that debt advisers were fully briefed on the long term implications of accessing pensions savings early.

Q11. Is there a case for introducing further flexibility in the trivial commutation rules?

and

Q12. What are the key barriers to transfer of small pots and are there any proposals from industry, consumer bodies or other interested parties as to how small pot transfers could be better facilitated?

We agree that there is a need for further flexibility in the arrangements as a whole and a level of harmonisation of the rules relating to small pots and to trivial commutation applying to trust-based and contract-based pension schemes. But the starting point seems to be more effective arrangements for individuals to keep track of the pensions they accumulate during their working lives and for small occupational pension pots to be amalgamated. We are not in a position to comment on any legal constraints on transfers, but it seems that there is a need for more information and affordable advice to be available to consumers about their pensions at the point they need it – such as when changing jobs. There is an argument that Government subsidy or sponsorship of advice would be money well spent in the long term if it ensured that individuals kept track of their pensions savings and made the right decisions about how they should be used.

Yours faithfully

Adam Phillips
Chair
Financial Services Consumer Panel