Consultation Response

FCA: Handbook changes to reflect the introduction of the Lifetime ISA

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About Age UK

Age UK is the country's largest charity dedicated to helping everyone make the most of later life. The Age UK network comprises around 150 local Age UKs reaching most of England. We provide information and advice to around 5.9 million people each year, through web-based and written materials and individual enquiries by telephone, letters, emails and face-to-face sessions. We work closely with Age UK Cymru, Age UK NI and Age UK Scotland.

About this consultation

The Lifetime Individual Savings Account (LISA) is intended to help people save for the purpose of providing a first home deposit, or for retirement. A LISA can be opened by an individual aged under 40, while payments attracting a government bonus of 25 per cent – equivalent to basic rate tax relief on pensions – can continue until age 50. Any money not used to buy a house can be withdrawn penalty-free from age 60, and if withdrawn before 60, certain charges apply. The FCA's consultation sets out a proposed approach to regulating the promotion and distribution of the LISA, and seeks specifically to address risks the LISA may present to consumer protection, under the headings of Complexity, Employer Pension Contributions, Investments, Access and Tax.

Key points and recommendations

- We broadly agree with the FCA's assessment of the risks to consumer protection posed by the LISA, and share the FCA's particular concern about the LISA's conflation of a short-medium term savings product with a long-term retail investment product.

- The LISA risks oversimplifying consumer perceptions about what makes for good retirement planning. It is important consumers understand that putting their money in a cash LISA and leaving it there until retirement may not produce an adequate retirement income, and that there are considerations for retirement saving and spending beyond the age of 60.

- On the basis of this concern, we identify a further element of risk in the category of 'Complexity', namely the impact of the LISA's design on retirement saving and income strategies, including beyond the age of 60.

- On risk warnings, we agree with the FCA's two proposals for the early withdrawal charge risk and potential loss of employer contributions to a workplace personal pension where a LISA is chosen instead.

- However, we consider the risk of savers neglecting retirement planning after the initial LISA decision, including by regular review and importantly after the age of 60, should also be expressly warned against.

- We propose that a comparative table is provided to consumers to ensure that the LISA government 'bonus' and workplace person tax relief are more easily compared.

1. Introduction

We previously set out our views on challenges posed by the LISA in written evidence to the Government's Pensions Automatic Enrolment Inquiry in April 2016, available at http://data.parliament.uk/writtenevidence/committeeevidence.svc/evidencedocument/work-and-pensions-committee/pensions-automatic-enrolment/written/31802.html.

We are encouraged to see the FCA acting to address some of the concerns we expressed there. Our headline concern regarding the potential impact of the LISA on pension adequacy remains, and is worth restating at the outset.

A retirement savings strategy should include at least an element of investment to allow for greater possible returns over the long term, and for lower susceptibility to inflation than would a purely cash-based retirement savings strategy. Around 80% of ISAs are held in cash.[1] Age UK is concerned that the perceived flexibility of the LISA, consumer familiarity with and trust in the ISA brand as a cash-savings rather than investment product, and the tendency of consumers to underestimate their retirement needs, may result in more people saving for retirement in cash only. This does not represent a suitable long-term investment strategy and we are concerned the LISA may thereby represent some risk to pension adequacy.

2. Consultation questions

Q2. Do you agree that the risk categories we have identified capture all of the relevant risks the LISA poses to our objectives? If not, which categories or risks would you add to or remove from our list?

Age UK broadly agrees with the five stated categories of risk to the consumer protection objective, and is pleased the FCA has given comprehensive consideration to the specific elements of risk in each category (at 2.8 and in Annex 2). We have identified two further elements of risk under 'Complexity' concerning (i) governance and (ii) consumer perceptions about the complexity of retirement planning, including beyond age 60.

(i) Complexity: governance

On the Complexity risk, the FCA sets out that *"investors may not sufficiently understand the differences between the features of a pension and a LISA in order to make informed decisions about the benefits and risks of each for their own circumstances."* Some of those differences are dealt with in the FCA's proposals and Cost Benefit Analysis (CBA).

We would add that governance arrangements and certain regulatory protections are important for delivering good outcomes for savers in later life. There is a risk that, under LISAs, consumers will not understand that pension governance and other regulatory

[1] HMRC (2016), ISA statistics

standards will not apply, which could lead to relatively worse outcomes in later life - for example, charge caps apply to default pension funds used for auto-enrolment, while there is no equivalent protection for a stocks and shares LISA.

(ii) Complexity: retirement planning perception

We are concerned that the LISA may oversimplify perceptions of what makes for good retirement planning, and ultimately result in a higher number of consumers 'underplanning'. This can include consumers failing to anticipate the need for a retirement income strategy, meaning spending their readily-available LISA cash too quickly after age 60. We consider this an important additional risk to the consumer protection objective.

It is established that people tend to underestimate their longevity, and make detailed retirement plans for the shorter term only (i.e. for the first year to five years of retirement).[2] [3] Although consumers may know that their retirement will comprise multiple phases of changing health and activity during which their financial needs will vary, the tendency nonetheless is to make a one-off decision about retirement finances as if it were a long and stable period of need.[4]

Against this background, the LISA's apparent overall simplicity (when compared with other pension products) and the attraction of its frictionless, tax-free and unlimited access to savings from age 60 diminishes much-needed emphasis on planning (and revising) for a long-term, sustainable and adaptable income in retirement. The risk is that investors fail to understand retirement planning as an enduring consideration and not a one-off decision, and that later life financial demands can be complex and changeable. The LISA's easy access to cash may thereby contribute to ill-planned decumulation and subsequently poorer retirement outcomes.

This risk appears to be considered at least in part by the FCA in its CBA, which states the LISA *"may hinder investors from adequately considering future retirement incomes in comparison to the more 'visible' wealth that can be accumulated in the LISA and other ISAs."* We consider this deserves greater consideration and should be addressed by risk warnings and disclosures at the point of sale, rather than waiting until retirement, in order to safely reinforce the idea that retirement planning is a life-long consideration, including after age 60.

Q3. Do you agree with our proposal to add guidance on information about risks that should be included when communicating with retail clients in relation to a LISA?

Age UK agrees with the FCA's proposals for risk warnings in respect of (i) the early withdrawal charge and (ii) potential loss of employer contributions to a workplace pension where a LISA is chosen instead.

A third risk warning: revising your savings strategy and planning beyond age 60

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2 Keohane, Nigel , 'How can we stop pensioners from underestimating their longevity and running out of money?', in *Ageing population and financial services*, Financial Conduct Authority (2016)

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

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In view of the risk to retirement planning perceptions we set out above, providers should also expressly warn consumers, at the point of sale, of the risk of inadequate retirement planning, including beyond age 60. The warning should be clear that there may different retirement planning considerations to be attended to at different times, such as:

- revising a LISA savings strategy regularly to ensure it aligns with changing financial circumstances or savings objectives (i.e. throughout the accumulation phase); and/or
- considering a retirement savings and income strategy beyond the age of 60 to ensure an adequate income throughout retirement (i.e. continued accumulation, and in decumulation).

Individuals' failure when engaging with the LISA to understand the long-term nature and different accumulation/decumulation considerations of a retirement saving may mean the the LISA delivers unsuitable outcomes for their needs in retirement. They should be warned to revise their savings objectives regularly and ensure they have a retirement savings and/or income plan beyond the age of 60.

Q4. Do you agree with our proposals to require LISA-specific information disclosures?

Revising a savings strategy and planning beyond age 60
We are pleased that the FCA proposes guidance for providers to include information about regular revision of a LISA savings strategy in their product information disclosures (draft COBS 14 Annex 1 2.3G).

As per the suggested risk warning above, the FCA should, at the same point, require providers to disclose information encouraging them to ensure a retirement income plan is considered for the period after they turn 60, to deter consumers from the view that planning ceases once their LISA cash becomes available.

This is in addition to the suggested third risk warning above, to ensure the entire package of information provided enables the best-informed consumer decision about whether a LISA is the right retirement savings product.

Tax
We are concerned that the presentation of pension saving via tax relief might seem superficially less attractive than the 'government bonus' proposed in LISAs. This risks steering people towards saving into a LISA, even where it may be a less suitable product for the individual.

We believe a tax comparison is essential and it needs to be made absolutely clear that a 25 per cent post-tax bonus is the same as pre-tax 20 per cent tax relief.

We have previously expressed our support for a 'rebranding' of pension tax relief, whereby plainer and more consistent terminology is used, to make otherwise confusing concepts of ‘relief’ and ‘government bonus’ more readily comparable.[5] We support the idea of re-branding pensions tax relief as a ‘government match’ or ‘bonus’ to counteract the risk of savers finding the ‘government bonus’ aspect of the LISA superficially more attractive, even though a 25 per cent post-tax ‘bonus’ is identical to a 20 per cent pre-tax ‘relief’. This should be explained up front in all forms of engagement with pensions and LISAs, alongside a clear indication of how a pension might benefit the individual over the longer-term.

In the promotion or distribution of the LISA specifically, a simple, generic comparison of the LISA government bonus as against tax relief on personal pensions - similar to the table proposed for comparison of different investment or savings returns at draft COBS 3.5R – would be effective to ease consumer misapprehension about a government bonus versus tax relief. Consumers do not typically understand pension tax relief, with many failing to realise it is a government contribution to their pension saving.[6]

MoneySavingExpert.com has published a LISA/personal pension tax comparison table, elements of which we consider would work well to enable consumers to make a better informed decision about which option is best for them.[7]

This would also bolster the risk warning on potential loss of employer contributions proposed in draft COBS 4.5.11G 2(b).

Q8. Do you agree with the description of the costs and benefits in our CBA?
Age UK agrees with the description of the costs and benefits in the CBA.

3. Conclusion

We accept that the flexibility of a LISA may be attractive, but this should not come at the cost of an adequate pension in later life. The FCA’s proposals for the promotion and distribution of the LISA will help to ensure investors are aware of the risks and complexities involved in adopting the LISA as a retirement savings vehicle, and especially where it is to the exclusion of other pension strategies and products. However, more emphasis is required in communications with clients to ensure the LISA does not distract savers from regularly revising their retirement savings plan, and ensuring their retirement planning does not stop at age 60.

It also important that the FCA works with HM Treasury to monitor the uptake of LISAs and the impact on pension saving, and to understand the impact that LISAs might have on income adequacy in retirement. It is imperative that people save into the right product to maximise the benefits of long-term saving.

5 http://data.parliament.uk/writtenevidence/committeeevidence.svc/evidencedocument/work-and-pensions-committee/pensions-automatic-enrolment/written/31802.html
6 Polling by YouGov for The People’s Pension in 2015 found 59% of people had heard of tax relief but did not understand what it meant, while 15% had never heard of it. Taken from Professional Pensions, 22 September 2015
7 Available at http://www.moneysavingexpert.com/savings/lifetime-ISAs as of 20 January 2017