



Institute
and Faculty
of Actuaries

MS14/3.2 Retirement income market study: Interim Report

Consultation response to the Financial Conduct
Authority

30 January 2015

About the Institute and Faculty of Actuaries

The Institute and Faculty of Actuaries is the chartered professional body for actuaries in the United Kingdom. A rigorous examination system is supported by a programme of continuous professional development and a professional code of conduct supports high standards, reflecting the significant role of the Profession in society.

Actuaries' training is founded on mathematical and statistical techniques used in insurance, pension fund management and investment and then builds the management skills associated with the application of these techniques. The training includes the derivation and application of 'mortality tables' used to assess probabilities of death or survival. It also includes the financial mathematics of interest and risk associated with different investment vehicles – from simple deposits through to complex stock market derivatives.

Actuaries provide commercial, financial and prudential advice on the management of a business' assets and liabilities, especially where long term management and planning are critical to the success of any business venture. A majority of actuaries work for insurance companies or pension funds – either as their direct employees or in firms which undertake work on a consultancy basis – but they also advise individuals and offer comment on social and public interest issues. Members of the profession have a statutory role in the supervision of pension funds and life insurance companies as well as a statutory role to provide actuarial opinions for managing agents at Lloyd's.



Eve Cinnirella
Financial Conduct Authority
25 The North Colonnade
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London, E14 5HS

30 January 2015

Dear Eve

IFoA response to the Retirement Income Market Study

1. The Institute and Faculty of Actuaries (IFoA) welcomes the opportunity to respond to the FCA's consultation on the retirement income market study. In preparing this response, we have consulted with some of our members who work in DC schemes, both as consultants and for providers, and some who have broader responsibilities within providers.

General comments

2. The IFoA is broadly supportive of the recommendations of the study. However, we would also encourage the FCA to undertake further research into policyholder behaviour. It is not evident that the proposed measures will always result in better outcomes for policyholders.
3. As evidenced in the FCA's thematic review of annuities, that increasing and improving product information does not necessarily change policyholder behaviour and lead to more people looking for the best outcome at retirement. While we support all initiatives to improve knowledge, policyholder inertia remains a significant challenge for the industry

Proposal 1 **We propose to require firms to make it clear to consumers how their quote compares relative to other providers operating on the open market.**

1A: **Whether the proposal could contribute to addressing the concerns we have identified?**

4. At face value the proposal appears to be a reasonable approach to addressing concerns. Providing retiring members with information should assist in them making the best decision. However, we are not convinced that simply providing information would meet the FCA's concerns about the operation of the market.
5. The provision of additional information would not necessarily ensure better competition. It is also unclear that the quoted form of annuity would be optimal for the policyholder. Different firms will take different approaches to the provision of enhanced annuities and the treatment of one underwriting factor may be different between firms, possibly resulting in the provision of an inaccurate comparison.

6. It still is possible that policyholders would only accept an option that is presented to them, rather than investigate alternatives in the broader market.

1B: How could the proposal be best implemented, and/or how could practical issues be resolved?

7. There are a number of limitations with the proposal that would require further work. Firstly, the provision of the additional information would have to sit within the guidance framework.
8. Annuities can be taken in many forms; therefore, there would have to be an established form of annuity that would be shown in the policyholder information. Any initial quotes provided may have to be in a standardised form; however, this approach would not necessarily meet the FCA's concerns about the functioning of the market. At the same time, there would have to be a clear indication that the information provided was not part of an annuity service.
9. Pricing in the annuity market can change rapidly. Policyholders would have to be aware that the quotes were indicative. A significant financial market event could result in policyholders receiving quotes at the point of retirement that would look significantly different to initial quotes provided. One option would be to point policyholders towards the guidance service for further information.

1C: What information could be feasibly provided over the phone and in writing?

10. Providing policyholders with different options for income by telephone could be counter-productive – given the inherent complexity of financial products - too many numbers with different meanings may be confusing for some policyholders. However, an indicative quotation followed with a statement suggesting that better quotations may be available from other providers would be a valuable message that could be delivered on multiple occasions through a telephony system. All oral quotations should be confirmed in writing.
11. As previous FCA examinations of the retirement income market have demonstrated, written communications do not lead to more people purchasing income from the open market. Where it is used, written communication should reinforce the existence of the guidance service.

1D: How the proposal could be applied to other retirement income products, for example income drawdown?

12. The new retirement market will require providers to indicate that there is a range of retirement income options. However, this should be undertaken well before policyholders reach the decision making stage, as we note in our response to option 3.
13. Any information supplied for other products should be clear about the specific risks.

2. We recommend to both the pensions guidance service and firms to take into account framing effects and other biases when designing tools to support consumer decision-making.

2A: Whether the proposal could contribute to addressing the concerns we have identified?

14. Developing a proposal that removes biases within an overall generic structure, but takes account of the risk appetite of individual policyholders, is likely to be a significant challenge. (the IFoA has suggested possible approaches in our response to option 3)

15. The IFoA would encourage the FCA to engage with all market participants in determining the nature of behavioural biases and to help refine the language that should be used in retirement communications.

2B: How the proposal could be best implemented, and/or how could practical issues be resolved?

16. As indicated in the previous paragraph, the IFoA would encourage the use of standardised simpler language that is understood by policyholders.

17. Communication of a 'rule of thumb' should emphasise that it is an average outcome. Communication to policyholders should encourage them to consider the likelihood that the average outcome will not be the outcome for a single policyholder.

2C: How the proposal could be applied to UFPLS or other products?

18. The IFoA would encourage all products to be subject to the same generic approach. Naturally, any language would have to reflect the differences between products, but the emphasis should be on removing jargon and industry terminology.

3. We will work with Government to develop an alternative to the current wakeup pack. Behavioural trialling of the wake-up pack would allow us to assess the impact on consumers' awareness of their right to shop around, and the number of people who exercise their open market option. We would like to hear from any firms that are interested in assisting us with this process.

3A: What should the proposed content of future at-retirement communications be?

19. The IFoA would encourage the FCA to consider communication at points before retirement. Initial retirement communication could be issued a number of years (rather than months) prior to retirement. Such communication would not set out retirement options in terms of income or product features, but rather pose a number of simple questions to policyholders about their intended lifestyle in retirement, expected expenditure and how they would finance that lifestyle and expenditure.

20. The purpose of such correspondence would be to act as an introduction to future short, but regular, communications that would reinforce some simple messages such as: the expected age of retirement, the possibility of living to advanced ages, the range of options available and the use of the guidance service. All the initial communication would aim to do would be to raise awareness of the issues rather than provide detailed financial information. The form of this communication could be generic rather than company specific.

21. Once policyholders are made aware of the potential challenges in financing retirement, they would then be in a position to take appropriate action. The IFoA recognises that even a period of 10 years before retirement for commencing such communication would not necessarily solve the challenge of insufficient retirement saving, but it would highlight the possible consequences of insufficient savings. If such an approach were to act as one of the incremental improvements for policyholder outcomes, as noted in our general comments, it is likely to be a valuable undertaking.

22. Introducing earlier engagement about retirement options could raise the issue of appropriate pre-retirement investment strategies. If policyholders intend to use the new pension freedoms, they could consider alternative investment options alongside future income requirements.

3B: Whether there is any other significant information that should be included in these communications? If so, please state the information required and why it should be included.

23. Policyholders should be aware of the implications of retirement income decisions on future tax demands and also any receipts of benefits in retirement. Providing this information well in advance of making decisions would allow policyholders to obtain the information they would need for better outcomes.

3C: Which aspects (if any) of the ABI Code we might consider incorporating into our rules in the pensions and retirement area? Please set out any additional measures that are not currently in the ABI Code that should be incorporated into our rules.

24. Rather than comment on specific rule changes, the IFoA would encourage the FCA to work with the Pensions Regulator (tPR) to create a level playing field for the retirement process for all pension scheme members, whether in trust or contract based schemes.

4. In the longer term, we recommend that a 'Pensions Dashboard' is created which:

- can be accessed by UK consumers at any time through a personal log-in
- sets out an individual's entitlements including all of their accumulated DC pension savings, and
- could be developed over time to allow consumers to view all of their other sources of retirement (such as DB and state pension entitlements) in one place.

4A: Whether the proposal could contribute to addressing the concerns we have identified?

25. The IFoA supports the introduction of a "Dashboard". There are many obstacles to overcome in creating such a piece of information; however, the operation of the Dashboard, alongside the increased communication could help address the FCA's concerns.

26. In an ideal environment, such an information mechanism should include all information relating to possible retirement income (DB, DC and State pensions). The challenges to achieve such an outcome are considerable; therefore, a complete Dashboard should not be an immediate priority.

4B: Whether, beyond those we have identified, you foresee any difficulties implementing this proposal?

27. There are many potential challenges to initial implementation, some of which we have noted below.

- The IT costs would be significant in supplying information and providing it to policyholders, so who would pay for them?
- There are Data Protection issues.
- Fund values may be provided at different dates.
- Unique identifiers for policyholders may not be readily available.

4C: How this proposal should be implemented and by whom?

28. Whilst we cannot comment on who is best placed to implement the Dashboard, we would encourage tPR and the FCA to consider how schemes and providers currently supply information and to whom. We would suggest that the Dashboard should be as simple to

operate as possible, particularly in the initial stages of operation. Use of existing information channels should be considered before a complex system is set in place.

5. We will continue to monitor the market and are seeking views on whether there are any particular aspects (in addition to those set out below) that we should monitor.

5A: The proposed monitoring activities set out above.

29. The IFoA welcomes the continuing monitoring of the market. As the retirement reforms take effect, it is important that the impact of the reforms are understood. There would be merit in understanding how the decisions of new pensioners have changed as a result of the introduction of additional options.

30. There could be advantages in understanding how different participants in the market elect to take their benefits. Therefore, some segmentation analysis may offer greater insight rather than an overall view of market developments. This may also provide some understanding to the areas in which policyholder inertia remains the greatest barrier to better outcomes.

5B: Any additional aspects that we should consider monitoring.

31. Policyholders with Guaranteed Annuity Options (GAOs) have a potentially valuable option. It would be useful to monitor the exercising and surrendering of the options in light of the new pension freedoms.

32. The IFoA would also welcome any monitoring of new products and how new pensioners intend to use them. While the retirement market will change over the next few years, understanding how policyholders react to the changes will be a useful indicator of whether inertia at retirement will continue.

33. If the FCA wished to discuss any of our comments in any further detail, you should contact our Technical Policy Manager, Philip Duggart, in the first instance. He is available on 01312401319 or at Philip.Duggart@actuaries.org.uk.

Yours sincerely



Nick Salter
President, Institute and Faculty of Actuaries