ASSOCIATION OF CONSULTING ACTUARIES

NEWS RELEASE

ACA SAYS GREATER FLEXIBILITY IN HOW RETIREMENT SAVINGS CAN BE USED IS KEY TO RENEW 'SOCIAL CONTRACT' BETWEEN GENERATIONS

19 December 2017: The Association of Consulting Actuaries (ACA) has responded to the consultation by the Intergenerational Commission, which is seeking solutions to the perceived growing gap in income outcomes across different generations. The ACA says from the perspective of renewing the "social contract" between generations, we believe that increasing flexibility in how traditional "retirement" savings can be used, could be an important part of that settlement, alongside a review of the intergenerational impact of pensions and wider tax reform. The ACA also says that retirement outcomes are likely to be improved by helping individuals to make realistic assessments of their expectations for retirement so that they can set appropriate savings targets.

The ACA's response[1] says given competing savings needs and an increasingly exclusive reliance on DC pension provision, many young people risk retiring on materially lower relative incomes than current retirees.

Steven Taylor, ACA Committee member and co-author of the ACA response alongside **Chintan Gandhi, Chair of the ACA's Younger Members' Group** commented, "we agree that many of the challenges of accumulating adequate retirement savings, such as competing savings needs, are not unique to the current generation and have been building for some time. However, in our view, these pressures have now reached a stage whereby many young employees are unable to save sufficiently or are put off from saving altogether."

"A graduate joining the workforce today faces University tuition fee repayments and rapidly rising rent. Combined with the challenges of saving for a house deposit or a holiday it is unsurprising that some young people might choose to prioritise other spending or saving above pensions – missing out on the longer-term benefit from their employer's contributions and the government's tax relief," **added Chintan Gandhi**.

The ACA response says the pressures will likely increase further if (as the ACA would like to see) automatic enrolment minimum contributions continue to rise. For example, the combined rate of 8% from 2019 is itself unlikely to be sufficient for most people to achieve the Pension Commissions' targeted replacement ratio of two-thirds (we estimate that over a 40-year career and assuming 3% real investment returns, contributions of around 16% would likely be needed to reach this benchmark).

Steven Taylor added, "given the significant financial incentives for retirement savings, e.g. tax relief and often generous matching employer contributions, the crowding out of retirement saving by shorter term needs should be a key area of concern for future public policy. In particular, for today's generation to save adequately for retirement, we believe ways must be found to allow young people to save flexibly, for multiple purposes, without disincentivising retirement saving.

[1] See http://www.aca.org.uk/files/ACA_response_to_Intergenerational_Commission_consultation-15_December_2017-20171215112846.pdf

"From the perspective of renewing the "social contract" between generations, we also believe that increasing flexibility in how traditional "retirement" savings can be used, could be an important part of that settlement. "

Possible Policy Responses

(i) Flexible Savings

One policy solution could be to introduce a 'National Flexible ISA' to allow withdrawals of up to £30,000 from pension saving in the accumulation phase – to fund house deposits or potentially other limited spending needs.

This complements flexibility of tax-free cash lump sums and withdrawals under Freedom & Choice in the decumulation phase, can be taxed consistently, and offered through existing occupational DC schemes (which the relatively complex Lifetime ISA is unable to do), without the need for extensive new legislation.

To ensure pension saving is restored after withdrawals, additional minimum employee contributions could be mandated for those who flexibly access cash in this way.

(ii) Pensions tax reform

In 2015/16, £38.2bn was received in pensions tax relief, with around two-thirds of this going to the 17% of the population paying higher or additional rate tax (and most likely to be towards the older end of the age spectrum).

Any of the major tax reform options (ranging from flat rate relief to pensions ISAs) that have been considered in recent years could result in a saving on this amount and hence achieve a positive intergenerational impact.

While the ACA makes no comment on which option is most appropriate, we recognise the importance of pensions and wider tax reform in renewing the "social contract" between the generations.

(iii) Realigning retirement expectations

In the ACA submission to the Cridland Report, we raised a number of policy concerns relating to State pension provision in an era where continued improvements to longevity have begun to challenge the concept of an agreed "retirement age". For example, although these macro trends are increasingly understood, at an individual level many young people still expect to retire at traditional ages (e.g. 60 or 65). We believe that retirement outcomes are likely to be improved by helping individuals to make realistic assessments of their expectations for retirement so that they can set appropriate savings targets.

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About the Association of Consulting Actuaries (ACA)

Members of the ACA provide advice to thousands of pension schemes, including most of the country's largest schemes. Members of the Association are all qualified actuaries and all actuarial advice given is subject to the Actuaries' Code. Advice given to clients is independent and impartial. ACA members include the scheme actuaries to schemes covering the majority of members of private sector defined benefit pension schemes. The ACA is the representative body for UK consulting actuaries, whilst the Institute and Faculty of Actuaries is the professional body.

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