

Life Academy lecture, Tuesday 17 November 2009

Is there a future for retirement as we know it?

An address by Trevor J Matthews

Good evening ladies and gentlemen, and thank you for inviting me to give this year's Life Academy lecture. It's a real privilege.

The title given to me is the question, "Is there a future for retirement as we know it?" My simple answer is, I jolly well hope not! When was the last time you read something positive about the future for retirement, based on where we are today? In fact, retirement is a relatively new concept that has rather sneaked up on us; it has emerged over time as an unintended consequence of many other factors.

A hundred years ago, the idea of retirement as a specific period of leisure was in no-one's mind. The vast majority of workers worked until they died, mostly in their 40s and 50s back then. There were very few hardy souls who simply wouldn't die, but couldn't live either, because of poverty. That's why Lloyd George famously introduced a state pension, of between 1s and 5s per week but it was never paid to the many but only to the few who were still breathing at the age of 70. He also introduced meanstesting, which is one of my pet hates today, but interestingly, the Lloyd George version was applied in the opposite way to today. Today, in general terms, meanstesting *triggers* a payment if a person's income doesn't reach a certain threshold, whereas back then, it *prevented* a payment if a person's income was above a certain level – 12 shillings a week to be precise.

That seems to make more sense to me. Does Simon Cowell or David Beckham really need the state to pay them an age-related pension? I'm pretty certain that introducing that type of meanstesting would be well received by the majority, and would free up some funds for more pressing needs.

However a lot has happened since the turn of the last century, so let's fast-forward a few generations. And I'm going to base my thoughts tonight around several words, all beginning with the letters C H.

The first one is **change**. One of the biggest changes of recent times is spontaneity. When I was a boy, life in general was pretty well devoid of spontaneity. It was instead routine and split into very defined periods. You went to school. You got a job. You got married. You had kids. If you were a guy, you stayed in your job. If you were a lady, you would look after the kids and the home. And if you survived to 65, the guy would retire for what all too often was a very brief period. Life was routine. Clothes were washed only on a Monday and ironed only on a Tuesday. Fish was eaten only on a Friday and roast beef only on a Sunday. Holidays always ran from Saturday to Saturday. Monday to Friday were known as working days because that's what they were, up until your 65th birthday when work stopped, and generally, life stopped soon after. Not much room for spontaneity.

Now I know that's an extreme generalisation, and there were plenty of exceptions, but that, by-and-large, was the rule for my parents' generation. Compare that with today. Education for some extends into their 20s or even their 30s. Working patterns are infinitely flexible. We eat what we like, when we like. We go where we like and do what we like. There's an infinite variety of pastimes and pleasures available around the clock and around the globe. Short breaks, career-breaks, job-shares, sabbaticals, gap years, 2nd and 3rd careers – these are all the norm now. Yet we still tend to look

at retirement as a fixed date in a calendar, after which life will change to something akin to 'pipe and slippers'. It's just not realistic. So we have to change, and that change has got to be far more imaginative than simply delaying the retirement start date for a number of years.

But before we consider change, I want to introduce my second C H word, and that is **cherish**. This is all about ensuring we don't throw out the baby with the bathwater. We should cherish all that is good about pensions currently, and do everything in our power to protect it.

Occupational pensions are not the silver bullet. They are complex; they are inflexible; and they are still uninviting to many. But they are the difference as to whether retirement years are happy or miserable for hundreds of thousands of people, and they relieve the state of a considerable financial burden. But there is danger on two fronts.

The first is the ongoing demise of defined benefit schemes. Yes, the costs are high. Yes, the risks are high. But is it really too late to save the concept? My own company has just been through the process of agonising over whether we could keep the DB scheme open to future accrual. The reasons not to are compelling and attractive, but in the end we did, and the wave of thankfulness from our staff has been both genuine and heartfelt. A good relationship between employers and employees will, I believe, become increasingly pivotal in financial planning, and I will explain more in a minute or two.

But I'm sad to see the DB scheme towel being thrown in so readily. How is it that the Dutch, for example, seem to have found a way to retain DB schemes, by a more imaginative approach to setting the level of benefits that makes some allowance for economic downturns. I think we can be too parochial in our outlook and it would do us good to learn from nations beyond this island. DB schemes in the UK still protect many thousands of people who work in the public and private sectors. They are worth fighting for. That said, the pressure on Governments to narrow the yawning gap, or to use another C H word, the yawning **chasm** between public and private sector schemes will, inevitably, lead to some tough decisions being made. I recognise that these will be put off for as long as humanly possible because they won't win votes; unfortunately, matters of integrity often don't.

The other danger is that the introduction of personal accounts will have the unintended outcome of eroding existing pension provision. It will force employers to take a long, hard look at pensions, and some will take that opportunity to switch their occupational schemes over to the personal account structure – the so-called leveling-down consequence. Auto-enrolment is a double-edged sword. In principle, it is a very good thing, and absolutely the right way to go. But it will add to employer costs as more people join, or rather, don't opt out of their schemes. We must not compound this by making the scheme-qualifying rules for self-certification so complex, and therefore administratively costly, that employers see the easy way out as being to close their schemes and opt for personal accounts instead.

As I say, there's enough downward pressure on good pension provision at the moment; the Government mustn't add to it. Whatever the rules, simplicity has to be the key. We all know that good quality pensions are not only important for people when they retire, but they are important to employers right now for attracting and retaining the good people they need to help their businesses flourish – and that is in everyone's interest, Government included.

By the way, if auto-enrolment is such a good thing, which it is, why not introduce it now on existing occupational pension schemes? I was talking to a colleague the other day who joined Friends Provident at 18 and is now approaching retirement with a prospective pension of two-thirds of his salary. What struck me was that he said that, to get that pension, he never had to make a single decision in the whole process. Enrolment to the scheme was a condition of employment but, he said, had he been given the choice at the time, he never would have joined and would have used the money he saved to put wide wheels on his Ford Anglia instead. But now, of course, he is so relieved that the decision was taken for him by others who knew better what was best for him. It seems an odd sort of human rights that stops the same good decisions being taken for people today.

This leads me to next C H word, which is **choices**. Compare my colleague's experience with someone today confronted with the option of joining a defined contribution scheme. The choices he or she has to make are: whether to join; when to join; what to contribute; when to contribute more; what funds to select; when to switch between funds; when to take the benefits and in what format. These choices are not necessarily informed choices at all, and yet will have a profound impact on the years after work. One of my own relations has just retired, having made firm plans about timing commitments and financial commitments, only to find that the retirement pot underpinning these plans suddenly lost a quarter of its value almost overnight.

This is truly devastating, and illustrates how the move from DB to DC transfers all the risks onto employees who, generally, are ill-equipped to handle them. Yet the irony is that we've presented employees with a multiplicity of choices to make, but not given them the fundamental choice about what financial vehicles could be harnessed to financial planning. We are still, in effect, assuming that a period of work will be followed by a period of retirement, and the two are separated by a single day of decision, and here's a vehicle that you can use, if you choose, to take you there.

And many will use it, and many will be disappointed. Why? Because it takes no account of how they want to live and what they need, financially, to enable that lifestyle.

Let's stay with personal accounts for a moment. I'm in favour of them because, provided the Government gets the rules right, and protects existing retirement provision, personal accounts will help a huge number of people to at least get a foothold on the savings ladder. But it is just a foothold, and it's absolutely certain that it won't provide an income which matches how people want to live their lives.

We know this from the Australian model which, although not perfect, has proved generally to be a success over a sustained period. At present employers pay 9% of salaries and employees on average pay an additional 3%. In Australia, the debate is how to lift contributions from the current level of 12% to something nearer 15%, recognising that current levels are still inadequate - yet they are already 50% higher than the maximum 8% under personal accounts.

And what makes the Australian model successful? Four things: It's compulsory; it's simple to understand; it's stable, having been around for some 15 years now; and people take an interest in it; they follow the progress of their retirement fund building up.

It's this last point – people taking an interest – that I believe is fundamental to the future, because the future has to be much more about financial planning than about

pensions. And so to my next CH word: **characteristics**. What will characterise the future, as far as the man and woman in the street is concerned?

I'd like to do a bit of blue-sky thinking here. What characteristics would I like to see? And these characteristics, of course, have to be set against the wonderful fact that people will live longer. Can I repeat that, because people living longer seems too often to be portrayed as an awful thing because it's going to somehow mess up the country's finances! It's not an awful thing. It's a wonderful thing, and we should celebrate it.

But the startling reality is that, under the current way of looking at things, some people will have more years in retirement than they spent in work. So let's carry on with my blue-sky thinking for a bit. Here are three things I want to see.

I want to see people who are happy. Being happy, of course, means different things to different people. Some people are happiest when they are working, some when they are travelling, some when they are socialising, and so on. It's not for us or anyone else to say 'this will make you happy'. We have to accept that this is for the individual to decide. And I know you may say that you can't buy happiness, and that's perfectly true, but the words of Mr Micawber from Dickens' David Copperfield novel still resonate today: "Annual income, twenty pounds, annual expenditure, nineteen six, result happiness. Annual income, twenty pounds, annual expenditure, twenty pounds, ought and six, result misery".

Secondly, I want to see people who are self-reliant. They know how they want to spend their lives in the future, but they know too what steps they have to take to make that happen. And whatever those steps are, I want them to be able to take them. I don't want to see them relying on the state or having to change their plans because the state, for whatever reason, has moved some goalposts.

Third, I want to see people who are free. Free from rules that overly constrain them for no apparent good reason. Free to work if they want to and how they want to, whether full-time, part-time, or just when they choose. Free to decide the best way for themselves to plan their own finances to fit in with their life-plans. Free to decide when they want to take the proceeds from their savings, and even free to decide when to take the state pension. Why not?

I worry that we sometimes get so caught up in the details that we lose sight of the big picture. But if, as a result of everything we did, our people were happy, self-reliant and free, we'd settle for that wouldn't we?

So what's the vehicle that will take us there? There isn't one! But I contend that we don't need a vehicle. Pensions is a vehicle – a good vehicle – but it's not enough. What we need is another C H word and that is a **chassis**. We need a chassis on which people can bolt all manner of savings contracts that suit them. What you would put on your chassis would be very different to what I would put on my chassis because where you want to get to will be different to where I want to get to. And so it will be for everybody.

I gave a speech just over a week ago and startled the audience by announcing that I was no longer in the pensions business, and that Friends Provident was no longer in the pensions business. But I went on to say that I am in the medium and long term savings business. That's the chassis I'm talking about. Pensions may well be one of the components that some people will bolt onto this chassis, but there will be many

other savings options for them to consider alongside pensions, such as corporate ISAs, Group Self-invested personal pensions, and sharesave schemes.

But there's an obvious problem, and let's use Defined Contribution schemes to illustrate it. Take up of employer-sponsored DC schemes is generally under 50% and can be as low as 5%. If people don't choose to join a DC scheme despite having the prospect of matched contributions and tax relief waved in front of them, then what hope have they got to be able to select appropriate savings plans to bolt onto their financial planning chassis? And the answer is, of course, no hope at all! But part of the problem is that they see the scheme in isolation to everything else. They haven't thought about the happiness, self-reliance and freedom scenario. All they know is that they have to hand over their money and 40 years later they will get it back with interest, but in the meantime, it's locked away.

As an aside, I heard the other day that the average level of arrears on houses being repossessed is just £5000. What sense does it make for a family to lose their home for the sake of £5000, which they may well have in their pension pot but which they can't get at because of the rules. I don't know who the rules work for but they certainly don't work for these families. The US allows people to take loans from their 401(k) funds and pay them back with interest. And in New Zealand, the KiwiSaver allows early access to pension savings under certain circumstances. We don't have to be as rigid as we are.

Anyway, it's time for another C H word and this time it's **challenge**. The challenge we face is how to present the happiness, self-reliance and freedom scenario to people in a way that is relevant, meaningful, believed and trusted? Well this is a huge challenge but there are two things we have going for us.

The first is technology. Technology enables us to educate and communicate with people in ways that nobody would have thought possible just a handful of years ago.

And the second is employers. Employers are already far more trusted than either the Government or the financial services industry. And they are coming to us and saying that they want more imaginative ways to engage with their workforce, to build relationships that breed loyalty and commitment.

Now, put these two together and we have a platform on which to build financial planning and really take it to a new level. And I use the word 'platform' deliberately because a corporate platform is what I'm talking about. What do I have in mind?

Imagine that you are an employee and you can go online in your workplace and not only see your employee benefits but also make changes to them. Imagine being able to make decisions about contribution levels and asset choices, based on illustrations tailor-made for you, and that reflect your very own risk-appetite rather than general guidance. Imagine having access to easy-to-use tools that enable you to explore different scenarios. Imagine seeing projections that really relate to you and your benefits. Or seeing the different tax implications or concessions that are available to you.

Imagine being presented with different savings options but at discounted costs, made possible by economies of scale. Imagine being able to transfer your savings between various product wrappers in a manner that maximises tax efficiencies.

Or imagine having a sharesave plan and being able to tip your maturing shares into a corporate ISA or a group SIPP, perhaps adjusting your investment choices to suit

your current circumstances or your future requirements. And imagine being able to do all these things yourself and know that everything you see is geared just to you.

You may be a young graduate in your first job; you can access online education tools to guide you on how to manage debt. Or if you haven't got a debt, the platform tools enable you to start putting some money into the corporate ISA, which appeals to you because, unlike a pension plan, you can get hold of the money at any time, yet it's still tax efficient.

Maybe you really enjoy your job and you want to know how your pension will be affected if you decide to stay on. Or maybe you want to work out what the best time would be to retire or to buy an annuity.

Or maybe you really don't enjoy your job, or you have commitments at home, perhaps caring for a loved one, and you want to know the options for flexible working; or for drawing down some of your pension and working part time; or supplementing your pension with an income from a share plan or a corporate ISA.

This is the world of the corporate platform – scenario planning, decision-enabling tools, advanced financial education, flexible products that are cheaper too. And all accessible online and tailored to you.

And what about from the employer's viewpoint?

It's clear that the pool of talented people to draw from will be smaller. The reason for this is another CH word, which is **childbirth**, or rather the lack of it! So in this shrinking market, you need to find some new and interesting additions to your employee benefits package so that you can attract and keep the people you need. The platform is an attractive answer, attractive because it will integrate with your existing benefits and systems; it will enable bulk upload of data, automation of salary sacrifice and payroll adjustments; it will handle much of your administration and reporting requirements; and most important of all, it will be relevant to every member of your workforce.

If you run a sharesave scheme, this will enable your employees to diversify out of company shares at some point to build a broader portfolio of equities. Or if you are managing pension assets for a big number of former employees, you're likely to welcome a system that can either administer this burden more cost efficiently, or perhaps enables you to transfer leavers to individual SIPP or ISA arrangements.

And in any event, you will certainly welcome the financial education tools to guide your staff through the personal decisions they need to make, and to lift the level of their financial management skills.

If I might throw in another C H word, it would be **chapter** because I am convinced that corporate platforms will open an exciting new chapter in employee benefits and financial planning, and I'm sure that they're going to play a very significant role in getting the UK saving again.

But I have to follow this up very quickly with another C H word – **chime** – because these platforms will only work if the way that the information is presented and taught chimes with what people – especially younger people – have come to expect from technology. The financial establishment is still guilty of concentrating on older people, using conventional methods, and simply patronising the young. We have to engage

in a way that is technologically savvy; in a way that is not only useful but fun and enjoyable too.

And behind the scenes, the tools that we build have to embrace what we can learn from behavioural science, such as how people react when presented with too many choices, and also what we can learn from the 'nudge' theory, knowing how to present decisions that need to be made in a way that makes it more likely that good and sensible decisions will result. Or to keep to our C H theme, that **chivvies** people in the right way at the right time.

Now you'll be pleased to know that there aren't many C H words left in the dictionary, but I do have three more to run through fairly quickly.

The first is **Chancellor**. Oh Mr Chancellor, please be aware of the damage you did by your budget decision to curtail tax relief on large contributions towards pensions. It was more about you playing to the gallery and certainly not helping to restore the savings culture. You have added unnecessary cost and complexity to pensions and, more disappointingly, you have sent out completely the wrong message to pension savers. Tax relief on contributions was a tangible way for all Governments of whatever persuasion saying to absolutely everyone, 'saving for your pension is a good thing and we will encourage it'. That unwritten contract was so important, but you have now broken it for one segment of savers, meaning you can easily break it for others sometime later. It was a poor decision. Ideally, I'd love you to reverse it, but I urge you not to make it the thin edge of a wedge.

And while I'm talking to you, Mr Chancellor, please please reconsider meanstesting. This seems so obvious but it simply cannot be right that potentially thousands of people, who can least afford it, use their hard-earned cash to pay into pension accounts, only to find at retirement that their efforts disqualify them from a range of state benefits, and that they would have been better off keeping their money in their pockets instead. I have repeatedly said, and I'll say it again, this is a scandal just waiting to happen, and it places our industry at potential risk of giving bad advice. If we are to encourage people to invest for their futures, and at the same time try to restore consumer confidence, then the benefits of doing so must be clear and simple. Meanstesting works against this principle and your position, Mr Chancellor, just has to mellow.

Which leads me to my second to last C H word, which is **choreography**. Those of us who watch John and Edward on The X Factor every week know what poor choreography looks like! There, it just makes us laugh, and we can laugh because it's not serious. But it is serious that the financial services industry and the Government get our choreography right.

Too often it feels like we are pulling in opposite directions. I'm thinking here not only of the chipping away at tax relief, but also what seems to be endless changes to pension policy, and indeed endless changes to pension ministers. If we go back to personal accounts as an example, the pensions industry already had tried and tested pension plans – the stakeholder model – and tried and tested administration systems. What we have now is two very different tracks running side-by-side towards what ought to be the same destination, but may not end up to be. As I say, we have to get this choreography right.

And so to my final C H word, and that is **charity**. I've been waxing lyrical about the need to engage with people and get involved with financial literacy and financial education, but there is one charity that saw this need long before most of us and has

done a huge amount to help literally thousands of people prepare for life beyond work – The Life Academy. Indeed, their change of name back in 2005 from the Pre-Retirement Association to the Life Academy was perceptively forward-thinking, recognising that retirement should not be somehow divorced from life itself. The rest of us are still playing catch-up.

I just want to say a very public thank you for the valuable work you do, and to say how proud my company is, and I'm sure I speak for many other companies too, about working with you to help us help others.

So there it is. Using our C H words, we've covered a lot of ground. We've thought about spontaneity being the **change** that needs to be addressed, but not at the expense of what is good already, which we should **cherish**. We've thought about **choices** and how they can be a bad thing when they are ill-informed. We did some blue-sky thinking about the **characteristics** we'd like to see – people being happy, self-reliant and free. We've recognised that a single-product vehicle is no longer appropriate, but that we need a **chassis** that each person can individualise to get us there. We know there are significant **challenges**, but technology and the workplace combined offer a solution, with corporate platforms opening a new **chapter**. The onus is on us to ensure that what we present to people **chimes** with what they expect and **chivvies** them to make good decisions. We've pleaded with the **Chancellor** to get on side and recognised that the **choreography** between the Government and financial services has to be better. And finally, we've acknowledged the great work of the **charity**, the Life Academy.

It only remains for me to say thank you, or in keeping with our C H theme, **Cheers!**