Institute and Faculty of Actuaries

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IFoA Budget Submission

The Institute and Faculty of Actuaries (IFoA) is a royal chartered, not-for-profit, professional body. We represent and regulate over 32,000 actuaries worldwide, and oversee their education at all stages of qualification and development throughout their careers.

Key points

- Fairness between the generations is rapidly becoming one of the most important issues in British politics and public policy discourse. It is especially important when assessing the economic impact of the coronavirus pandemic and the decisions the Government makes about the UK's recovery from Covid-19. A long-term view is essential if we are to meet the needs of UK society, without placing an unfair and unmanageable burden on younger, and future generations.

- When making decisions about charting the UK's recovery from the pandemic and its new role outside of the European Union, it is vital that the Government ensures that economic impacts and risks are shared and managed across society, and across generations, in a way that is fair and manageable for all. It is a matter of public interest that the stability and durability of the financial system is maintained.

- The 2021 Budget will set the tone of the UK's recovery from the pandemic. The IFoA therefore urges the Chancellor to use the fiscal levers at his disposal to heal the intergenerational divide in the UK, by harnessing the Government's levelling-up agenda to address the disparity in fairness between generations.

Should you want to discuss any of the points raised please contact Katy Little, Policy and Public Affairs Assistant (katy.little@actuaries.org.uk) in the first instance.

Retirement & Wealth

1. The evolution of retirement saving across public and private pensions has contributed towards an intergenerational imbalance, long before Covid-19 hit. The move from DB to DC pensions as the main form of retirement saving in the UK over the past decade has shifted the responsibility for retirement security from employers and the state to individuals. In the world of pensions and long term savings, the economic impacts of Covid-19 will mean different things to different people.

2. In a statement to the House of Commons on 11 January the Chancellor noted that, on aggregate, the household savings ratio reached record levels during the pandemic. But this has not been felt equally across generations. Whilst younger working-age adults were the most likely to have increased the amount they saved each month during lockdown, a survey by Paragon found those in the 18 to 24 age category were also two times more likely to have withdrawn money from savings to pay for essentials.[1] One of the main factors causing people to dip into their savings has been the rise in job insecurity. Individuals affected by unemployment, under-employment, or placed on the Governments furlough scheme during the pandemic are more likely to be younger workers and those on lower incomes. A recent FCA survey reported that a higher proportion of Millennials and Generation-X are working in 'Covid-impacted' sectors.[2]

3. Conversely 50-64-year-olds were the most likely (among those of working-age) to have reduced their rate of saving during the pandemic.[3] Middle aged workers tended to have more security in their jobs, with the Government website showing that workers aged 49 were least likely to be furloughed.[4] But those reaching the end of their working lives have also been disproportionately affected by redundancy, and at higher risk of furlough. There are a significant number of individuals now using pension freedoms to withdraw pension funds earlier than planned. Whilst this may help alleviate short term financial pressures, it is reducing savings for retirement, leaving many more people exposed to the risk of financial difficulties later in retirement, and the need to draw on welfare support funded by younger working taxpayers.

4. There is also a stark divide between housing wealth between generations. Primary housing is the largest component of wealth held by older households in the UK. The ability to draw on housing wealth is a key factor in financial security, spending power and paying for social care in retirement. Generally speaking, younger cohorts of the working generations tend to have better access to cash, but are struggling to access the housing market and build housing wealth. With interest rates at an all-time low, people with cash savings are struggling to reap any benefits even if they are managing to put more money away. This coupled with the lack of affordable housing available for first time buyers means that younger generations may never be able step onto the housing ladder and build housing wealth to support them through retirement. The Resolution Foundation estimates it will take the typical first-time buyer 21 years to acquire enough capital in order to put down a deposit on a home. [5]

5. As the full economic impact of Covid-19 remains to be seen, it is imperative that the Treasury takes this opportunity to re-set the UK's economy to ensure that spending and tax decisions benefit the long-term financial wellbeing of all cohorts of the population. This is a difficult balancing act and is

[1] https://www.themoneypages.com/saving-banking/big-spenders-generation-z-splash-cash-lockdown/
[2] https://www.fca.org.uk/insight/coronavirus-and-intergenerational-difference-emerging-picture
[3] https://www.resolutionfoundation.org/app/uploads/2020/10/Intergenerational-audit-2020.pdf
[4] https://www.gov.uk/government/publications/coronavirus-job-retention-scheme-statistics-july-2020/coronavirus-job-retention-scheme-statistics-july-2020#demographics--age-and-gender-breakdown
[5] https://www.resolutionfoundation.org/app/uploads/2020/10/Intergenerational-audit-2020.pdf

likely to remain so for some years but long term impacts on cross-society and inter-generational equity should be key considerations in all Government spending ad fiscal decisions.

GMP equalisation

6. Beyond the generational differences that exists within the pensions landscape we know that there also exists gender imbalances. For the purposes of the Budget, we would ask that the government, as a first step, fulfils its commitment on providing clarity on conversion of Guaranteed Minimum Pensions (GMP) to regular scheme benefits.

7. GMP is a specific amount of pension and is payable at age 60 for females and 65 for males. Historically, the amounts and ages were set out by the state to occupational schemes in substitution for the earnings-related part of the similarly sex-specific state pension.

8. The High Court's Lloyds Banking Group judgment in October 2018 confirmed that pension schemes needed to pay equal benefits to men and women despite any sex-specific "Guaranteed Minimum Pensions" (GMPs) built up between 1990 and 1997. The subsequent equalisation required is complex, and may be achieved by a number of different methods. Since then, HMRC have issued guidance on some of the tax implications of GMP equalisation however, there is still a large area of uncertainty, particularly, but not exclusively, in the guidance in terms of GMP conversion. The Government consulted on improvements to the legislation in 2016, yet no changes have been made.

9. The resulting delay of clear guidance means that thousands of schemes are struggling to pay millions of members the benefits they are due because of the uncertain tax framework. As a result, many trustees and their legal advisers are struggling to move forward and may end up taking a sub-optimal decision for their scheme in order to avoid conversion.

10. The IFoA would ask that the Government to take steps at the upcoming Budget to clarify, and if necessary bring forward legislation, so that advice can be provided to trustees to allow them to pay pension scheme members their correct benefits. Failure to do so could delay equalisation for many years, and continue to negatively impact on the level of benefits members receive.

Climate Change

11. The effects of climate change present a number of threats for future generations. Actions today will have a very large impact on future risks as a lack of action, combined with the non-linear nature of climate systems, may make some future changes irreversible and potentially unmanageable. That is why the Government has made ambitious commitments to reach net zero by 2050. Green Climate Change is perhaps the biggest the risk to future generations wellbeing, and Green Finance has a vital role to play, as fuelling the transition to a sustainable and inclusive global economy will require significant amounts of capital.

12. In the wake of Covid-19, there is an opportunity to put green finance at the heart of the economic recovery. Not just to meet the ambitions, but secure a just transition and a strong economic future. As the Government looks to stimulate the economy as it recovers from Covid-19, it is essential that the Government's spending priorities align with its net zero goals in order to accelerate the transition to a low carbon economy. Securing an orderly market transition to a lower carbon future will necessarily involve many different actors. The Government must seek a just transition, with Green Finance and the environment at the heart of reshaping the UK's economy. A shift is required to align the objectives of the financial system with the UK's net zero commitments. This will require a collaborative effort from policy makers, regulators and industry to create incentives to organise and direct capital towards green products.

13. In the year that the UK hosts COP26, the Government has an opportunity to demonstrate it is a world leader in championing the growth of green finance and a green recovery. The Chancellor should consider putting Green Finance at the heart of the Government's spending programme to reinvigorate the economy at the upcoming Budget.

Social Care

14. The pressures facing the health and social care system are well-documented, and are largely driven by the UK's changing demographics. The population is growing, individuals are living longer, and there is a growing proportion of older people. In mid-2016 there were 1.6 million people aged 85 and over; by mid-2041 this is projected to double to 3.2 million.

15. The UK's ageing population will continue to increase pressure on public services, as the number of people using these services exceeds those paying into the system through general taxation. Social care is facing high growth in demand, the cost of which is projected to rise by around £12bn by 2031, growing at an average rate of 3.7% a year. At the same time, projected growth in spending on social care is just 2.1% a year. This has left a funding gap of £1.5bn in 2020/21 and £6bn by 2030/31.

16. Failure from Government to properly address the increasing cost of the UK's care needs will only result in increased pressure on public services, at a time where Covid-19 has already tested the limits of the UK's healthcare system. The IFoA strongly urges the Government to act sooner, rather than later, to look at sustainable funding solution to address the long term need of the ageing populations. The intergenerational question surrounding social care is not should we spend more, so much as who should foot the bill.

17. As pointed out by the Lords Committee on Intergenerational Fairness, the number of retired people who receive more from the state than they pay in taxes will grow as this age group increasingly requires medical treatment and social care. If the increased costs of later life for a growing older population were to be paid for simply by increasing the rates of existing taxes then it would be primarily paid for by working age households. If no action is taken, then the costs of this spending will be added to the national debt, greatly increasing its size from its already enlarged state. This is not sustainable and the costs of servicing and repaying this debt will be borne by younger generations and the unborn.[6] This means that it is reasonable that at least some of this increase in costs should fall to the current generation of older people.

18. A range of funding options will be needed in order to solve the crisis in a way that is truly intergenerationally fair. This might include one solution for those already in retirement, or with care needs, and one for the working population with potential future care needs. It is unlikely that there will be a universal "silver bullet" product solution. We note there are a range of both insurance and savings-based financial products that already exist on the market that government should consider to be suitable for certain parts of the working population, depending on their wealth, assets, risk appetite and health. These include, immediate needs annuities, lifestyle insurance care riders, retirement income options made available by the "Freedom and Choice" and Equity release or other property-based solutions.

19. High levels of government spending will not guarantee affordable access to social care, and increased levels of spending are likely to become unaffordable for government over the longer term. The UK remains one of the only developed countries not to have implemented an insurance or cost

[6] https://publications.parliament.uk/pa/ld201719/ldselect/ldintfair/329/32902.htm

sharing initiative to address the issue of social care. The Government should look reasonably at what it can provide for individuals, now and in the future, to support the UK's ageing population.