

# **Memorandum Submitted to the Treasury Select Committee by the Resolution Foundation**

## **1. Executive Summary**

1.1 The Resolution Foundation welcomes the Treasury Select Committee Inquiry into Financial Inclusion as timely and important.

1.2 The focus of this submission is on the vital and challenging issue of access to financial advice, particularly for basic rate taxpayers on less than average income. They have both the most to gain from getting financial decisions right and the least access to help in doing so. They are excluded from advice because they tend not to be economically attractive to target with products, and advice comes bundled with products.

1.3 Today, some one in three of the UK workforce – more than eight million basic rate taxpayers - live in an advice “exclusion zone”, with little or no access to financial advice. Partly as a result, consumer debt is spiralling and more and more of citizens face a grim future of dependence on the state. Against this background, the Resolution Foundation believes that the time has come for the Government and the private sector to work together to close this advice gap and to create a new national financial advice resource.

1.4 The Resolution Foundation is a research and policy organisation which aims to provide new thinking on how people with below average earnings can access and use the financial services system. It is focusing particularly on how the advice needs of people earning less than the national average, but above the level on which they are wholly reliant on state benefits, are met either by the public or private sector. It also focuses on how such individuals can navigate successfully their most important financial decisions, and will explore how improving the quality of financial decision-making among this group can have a measurable impact on future welfare costs.

1.5 Given our areas of interest, we wish to make an informed contribution to the public policy debate around financial inclusion and to assist the Committee’s consideration of these issues. While our particular focus is on access to financial advice, we also have an interest in incentives and barriers to saving for people on below average incomes, as well as in the role of Government and other bodies in promoting financial inclusion.

1.6 The Foundation is working intensively with Government departments, the Financial Services Authority, voluntary groups, consumer stakeholders and the financial services industry in an attempt to catalyse agreement on the key issues and on possible solutions. We have also initiated a programme of research, which includes new research to understand better the financial decision-making behaviours of affected households. Early findings will be available at the beginning of February 2006. Other research includes costing the value of poor financial decision-making to the individual and the state and developing proposals for how a national advice resource could work in practice.

1.7 We would be pleased to give oral evidence to the Committee if asked to do so.

## **2. The Resolution Foundation**

2.1 The Resolution Foundation is a not-for-profit, non-party political, organisation and is committed to producing the highest quality socio-economic research into the issues of generic financial advice, together with practical proposals for action, capable of implementation by Government and industry.

2.2 The Foundation is chaired by Clive Cowdery, who is also Chairman of Resolution plc and its Chief Executive is Sue Regan. The Foundation has a Board of Trustees which includes Baroness Greengross.

2.3 The Foundation is privately funded, with no revenue from government or groups within the financial services industry.

## **3. Background**

3.1 There are around 8 million people in the UK today who pay basic rate tax on incomes between £10,000 and £22,060 per annum. Both figures are significant – the higher is the national average income and the lower is the threshold from which people are deemed to start becoming independent of state support. It is a large group consisting of more than a third of the full-time workforce.

3.2 Basic rate tax payers with this level of income largely fall outside of the catchment criteria for financial advice in the UK. Most free advice services cater to the remedial needs of unemployed people or those already in serious debt. Meanwhile, the financial services industry offers advice only when bundled with a product sale. At these income levels, such sales are just not attractive to most product providers who focus on the most profitable customers – i.e. those on higher incomes.

## **4. Our Aims**

4.1 The Resolution Foundation believes that it is in the interests of all stakeholders (the individuals concerned, the state, and the financial services industry) that the 8 million basic rate tax payers currently without access to financial advice are better served. To support this aim, we have three goals:

4.1.1 firstly, to examine the rapid development of a new national financial advice resource funded through a public/private partnership, which will make broad and impartial advice on all important financial decisions at the point of need

4.1.2 over the medium-term, to design and promote new ways for individuals to connect optimally their housing, credit, saving, and pension

decisions in order to maximise their opportunities of creating future financial assets

4.1.3 in the longer-term, to support the work of other organisations in critical areas including financial education, and reforms of the product, fiscal and regulatory framework

4.2 On a limited income, this group of 8 million people needs to deal with financial complexity in daily life, such as:

- housing options
- student loan repayment programmes, dovetailed with earnings capability
- credit options to finance necessary purchases
- life events such as unemployment, sickness and divorce, requiring a mix of basic protection and savings programmes with continued access to state resources
- pension decisions, reflecting employer options, individual choices, and state-sponsored schemes as they evolve in the next few years
- steps taken immediately prior to retirement, which can significantly improve income and access to capital in older age.

4.3 The Resolution Foundation understands the importance to individuals of making financial decisions. This understanding has derived from the activity of Resolution plc, which serves millions of investors who have made past contributions to life assurance funds which subsequently closed to new business. However, the Resolution Foundation is privately funded and its views cannot be taken to reflect the views of Resolution plc.

## **5. The advice gap**

5.1 It is particularly important that people in this group make their financial decisions carefully. Yet many of the 8 million are not well placed to do so. Most have low financial awareness. Although the financial services industry spends more than £1 billion promoting various products and services, there is a need to provide clarity and direction that cuts through the noise.

5.2 Crucially, few have access to the kind of impartial advice, guidance and expertise that would help them to get the key decisions right – at the time they need to make them.

5.3 There is already a range of initiatives that will benefit this group in the long run, including the Financial Services Authority's Financial Capability Programme. Others, like the Product Simplification Campaign, chaired by Ron Sandler, will be of some benefit in the short term. The industry is also playing its part.

5.4 This advice gap matters hugely to individuals and to the state. By making bad basic decisions – for example, by using available money for saving whilst leaving expensive borrowings in place – individuals do themselves long-term financial harm. This will be a financial cost to the state, if not immediately then in

the future, when people who have made inadequate provision will be thrown back on the public benefits system.

5.5 The Resolution Foundation is currently calculating the cost to the state of bad financial decisions. We will argue that this cost could be greatly reduced by a new national resource, structured as a public/private partnership, spending a fraction of state savings annually on providing impartial advice at the moment a critical financial decision is being made.

## **6. Can the financial services industry fill this gap?**

6.1 The financial services industry today offers advice to the higher income population as part of a package that includes sales of products by banks, life insurance companies and limited availability of paid-for advice.

6.2 In the past, basic services were also available to prudent households, through trusting relationships with, for example, high street mutual building societies, to encourage saving as the first step towards home ownership. Additionally, door-to-door service was delivered by more than 20,000 insurance agents serving the community.

6.3 The landscape has irreversibly changed. The basic, community-style service has gone and our target group of 8 million basic rate tax payers is unprofitable for the financial services industry. We call this the advice 'exclusion zone'.

6.4 The financial services industry is not just a major contributor to the British economy, it is also a vital stakeholder in social welfare. In recent years it has made significant improvements in competitiveness, and thus the value delivered to consumers.

6.5 It is unrealistic to expect industry to return to the old model of broad service funded by higher margin products. Instead, in a mixed economy, a partnership between industry and government across all income groups is needed to address this public need for advice.

6.6 The Resolution Foundation is committed to exploring such a public / private partnership as a way of closing the advice gap.

## **7. Next Steps**

7.1 In pursuing its goals, the Resolution Foundation has begun to:

- commission independent research into the most important life stage decisions people make, and to cost fully the value of a good or bad decision both to the individual and to the state

- consult widely with voluntary groups, the Government, the Financial Services Authority, trade unions, employers and the financial services industry on how best to tackle the infrastructure gap for impartial advice
- develop some early drafts of concrete and fully-costed proposals for how a national advice resource might work in practice
- examine how such a solution might be implemented and funded either by Government or industry or both.

7.2 The Resolution Foundation plans to facilitate a forum for all interested parties to share perspectives on the advice gap and to discuss possible solutions for inclusion on the agenda of Government and the financial services industry. This will start with a conference scheduled for February 2006, which will also provide an opportunity to examine initial outcomes from current Resolution Foundation research activities.

7.3 As well as providing a comprehensive review of the current state of progress towards enabling better financial decisions, a holistic plan may emerge allowing all interested parties to move towards action rather than prolonged analysis.

## **8. Action is needed now**

8.1 Inappropriate financial decisions are being made every day. The future impact of these decisions seriously hampers those on marginal income from accumulating assets over their working lives and accrues a future cost to the state. Unless addressed, this situation will deteriorate:

- with the financial services industry spending over £1 billion on promoting its products, confusion continues to grow
- consumer debt, already over £1 trillion, continues to increase with the potential for devastating personal impact
- pension reform is necessary but has the potential to add to personal confusion or, even worse, lead people to believe their financial problems are resolved.

8.2 The Resolution Foundation believes passionately in the need for urgent action to establish a public private partnership in order to ensure the widespread availability of life-changing financial advice for those who need it most.

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