CSFI
Centre for the Study of Financial Innovation

PENSION INSURANCE CORPORATION

Advice on our new pensions “freedom”: a round-table in the CSFI/PIC pensions fellowship programme, with Michelle Cracknell (Pensions Advisory Service), Robert Gardner (Redington), Jamie Jenkins (Standard Life) and Mick McAteer (Financial Inclusion Centre).

Held on Wednesday, June 18, 2014, from 12.30-2.15pm.
At the offices of SWIFT, The Corn Exchange, 55 Mark Lane, London, EC3R 7NE.

CSFI PIC Pensions Fellowship Programme

The round-table was set up to discuss the government’s promise of advice for everyone at the point of retirement, so that they can exercise their new “freedom and choice in pensions” wisely. But every factor, from individual circumstances to the bewildering choice of products and the cost of advice, makes these decisions difficult.

Hence the need for guidance and advice: the distinction is an important one. The promised guidance will be free for, say, a 25-minute slot at the point of retirement. Advice could cost £1,000. Focused, or simplified advice – on tax, for instance – might come in at £300; digital diagnosis at £150.

Guidance will encourage people to think about issues in the round eg debt levels, entitlement to state benefits, ability to defer a pension. It will signpost people to the next step, which might include paid-for advice from a regulated IFA. Guidance means there are no definitive recommendations – just all the things you should think about in planning for retirement.

The potential demand, from April 2015, is estimated at 400,000 people a year. The take-up rate is expected to be 20-50%. (PAS currently deals with 80,000.) It could cost £7m-£8m a year for each to be given a 25-minute interview by a pensions specialist.

It would be easier to understand people’s circumstances if there were a central repository of data about a person’s financial state, and maybe even health. This supports the case for a central utility delivering guidance.

The immediate problem is that so few people are “retirement ready”. This should improve as the next generation benefits not only from financial education but (hopefully) from a se-change in culture. People will be talking about their pensions/savings, encouraged by a series of interventions.

Then there is the huge range of individual circumstances, eg:
Level 1: approaching retirement with a mortgage and credit card debt
Level 2. no debt but no pension pot either
Level 3. some wealth accumulated – but may not be aware of it.

Different advice is needed for each level.

Plenty of scope for online guidance. A parallel was drawn with online self-diagnosis in medicine. Wealth Wizards, an online service, has been approved by the FCA. Aegon has Retiready, a digital “retirement readiness” service.

Having been auto-enrolled into pension saving through inertia, in contrast, engagement is needed in the decision(s) on what to do with the eventual pot.

Two extremes: take it all as cash or buy an annuity. The main problem with an annuity is that it is irreversible. Cashing in will probably make sense for small amounts. However, even with £30,000 tax issues can be significant.

In the middle? Drawdown. Some of the options may look like a bank account, others like an investment fund; they could be insurance or investment based. Advice is needed, but there is a big gap between free guidance and the cost of independent advice.

Will there still be a role for annuities? Between, say, 60 and 75, you could take an income product with a higher level of income than an annuity. Yes it would have some investment risk. Different solutions may well be needed at different points in retirement. A deferred, or a short-term, annuity may be part of the answer. So is working longer.

Government policy carries some big risks. The annuity market needed reform – to commutation; the ability to aggregate small pots; freedom above a certain income level; flexibility over when you buy it – but not a deathknell.

The reforms do not deal with the low-value annuity problem – you can get a higher income only through exposure to market risk and drawdown risk (ie you will run out of money before you die). The annuities that remain will be damaged by the removal of cross-subsidies.

There are concerns about product design and governance as the asset management industry produces innovative products, as well as the additional advice costs. The additional costs will come out of pension pots, so you will need to save more to generate the same level of guaranteed income.

The guidance guarantee is not enough, what matters is access to advice generally. Focused advice – yes, but this is predicated on an effective filtering stage that covers mortgages, investment, tax, entitlement to benefits, long-term care.

The danger is that the pensions hook will lead to inappropriate cross-selling of products by the financial services industry.

Sincerely yours,

Jane Fuller
Co-director/CSFI PIC Pensions Fellow