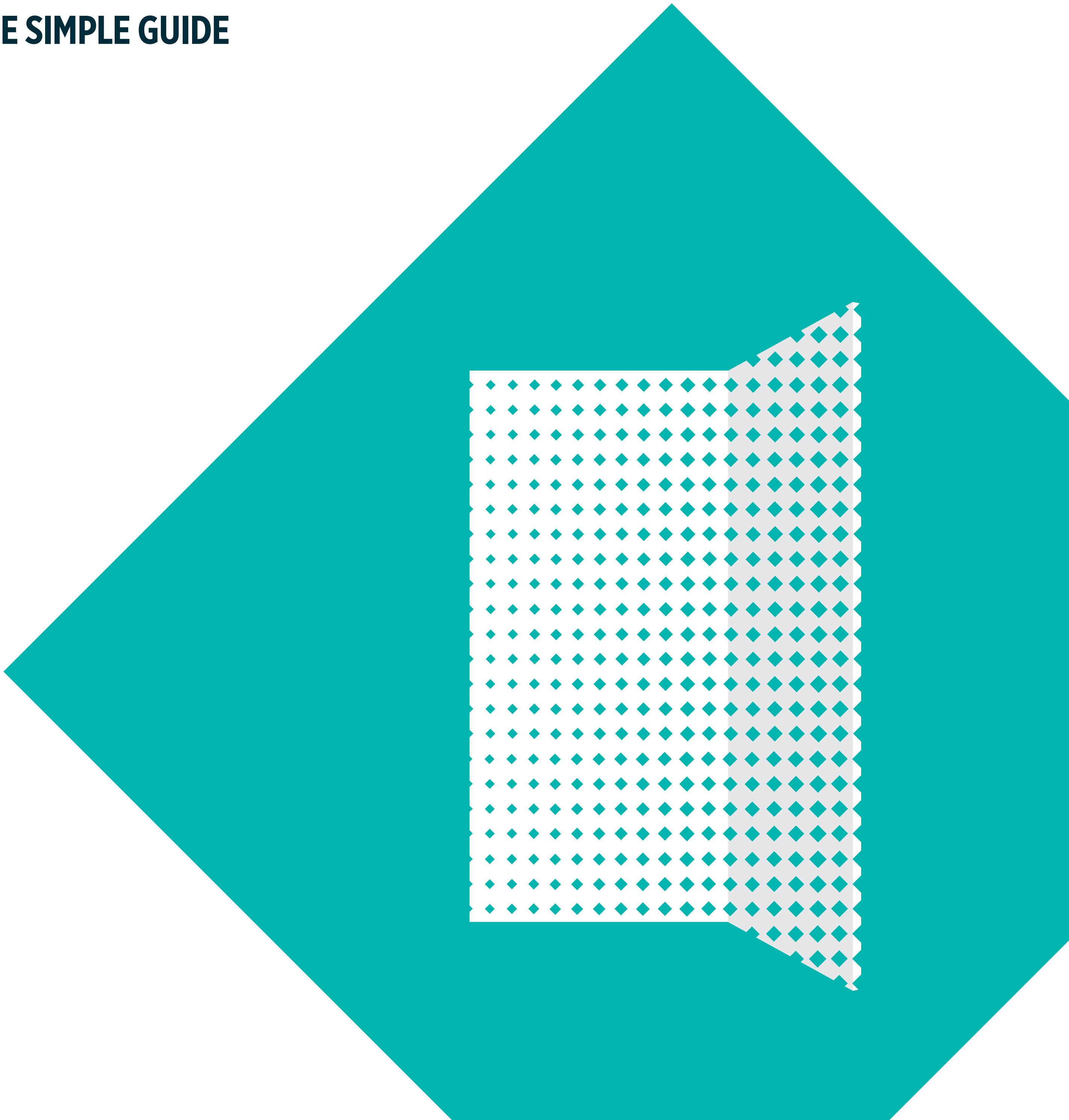
PENSIONS AND
LIFETIME SAVINGS
ASSOCIATION

December 2015

AT RETIREMENT SERVICES

MADE SIMPLE GUIDE



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Please note that references to Pensions and Lifetimes Savings Association research was published under our previous name of the National Association of Pension Funds

FOREWORD

AN EDUCATED PATHWAY TO RETIREMENT INCOME

SINCE THE LAST MADE SIMPLE GUIDE ON PROFESSIONAL AT RETIREMENT SERVICES WAS PUBLISHED, A LOT HAS CHANGED.

Who would have imagined the breadth and scale of the changes to our pension system announced in the Budget of March 2014? Freedom and choice in pensions was the most seismic change in our pension landscape for a generation and due to this, there is a set of challenges and choices that will fundamentally affect all those with defined contribution (DC) schemes who are approaching retirement and their well-being in later life.

This Made Simple Guide gives employers and trustees an insight into how the pension changes have affected the retirement income options and choices for pension savers. It identifies the help and support they can offer savers for what the Pensions and Lifetime Savings Association has highlighted as 'the growing unpredictability of retirement and complexity of making a very different set of decisions about what to do with their retirement savings' – providing savers with an educated pathway to their retirement income.

Jonathan Watts-Lay
Director, WEALTH at work

FREEDOM AND CHOICE WAS THE MOST SEISMIC CHANGE IN OUR PENSION LANDSCAPE FOR A GENERATION

1
INTRODUCTION

SINCE THE LAST MADE SIMPLE GUIDE DEALING WITH AT RETIREMENT ADVICE AND GUIDANCE, A LOT HAS CHANGED. TWO YEARS AGO THE TYPICAL OUTCOME FOR A DEFINED CONTRIBUTION (DC) PENSION SCHEME MEMBER WAS TO TAKE THEIR TAX FREE LUMP SUM AND PURCHASE AN ANNUITY WITH THE REMAINDER OF THEIR PENSION FUND.

Many used the 'open market option' to get an annuity rate that took account of their health and lifestyle and obtained the best rates available in the market at the time; however the majority did not, choosing to remain with their existing pension provider. Extensive consumer research and a review by the Financial Conduct Authority (FCA) concluded that the annuity market wasn't working well for pension savers and that change was needed.

What few imagined was the breadth and scale of the changes to our pension system announced in the Budget of March 2014. Freedom and choice in pensions was the most seismic change in our pension landscape for a generation.

Options previously unavailable for the majority of retirees such as flexible income drawdown were announced ready and available to DC pension savers from April 2015, with unfettered access to all from the age of 55.

Annuity sales halved overnight and signalled a significant evolution to the nature of the UK's retirement market.

While this freedom and flexibility has been broadly welcomed by pension savers and professional pensions practitioners alike, there is no doubt that the retirement income decisions that DC members now face are far more complex than they were before that Budget. Rather than a simple journey from pension saving into an annuity, savers must now contemplate a set of challenges and choices that will fundamentally affect their well-being in later life, including;

- When to access their pension savings, if at all.
- Whether to turn their savings into an income secured for life or take on board a new range of risks and draw a flexible income from their pension pot.
- How to use pension savings alongside other lifetime savings such as ISAs to make the most of generous new tax allowances and inheritance opportunities.

These challenges are not just the concern of the pension saver; employers and trustees will see their roles develop from being more than the provider and custodian of a valuable employment benefit. They have new challenges themselves to deal with; transfers from defined benefit (DB) schemes are expected to increase as savers seek to access the flexibilities inherent in the DC framework and employees already embracing flexible working patterns, may view their pension as a mid-life financial lifeboat to be accessed in their 50's, as much as an income replacement vehicle supporting a lifestyle from a 'normal' retirement date.

But some things haven't changed. For example;

- Employees still want to look forward to a retirement offering more 'me time' and a comfortable financial position.
- Employers will still support those employees saving towards retirement throughout their working lives with some form of workplace pension.
- Trustees still have a responsibility to support scheme members through their retirement journey with a retirement process that helps them receive a good outcome from their pension savings.

2
THE MARKET: THE BACKGROUND

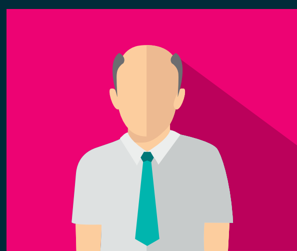
IN RECENT YEARS, RETIREMENT HAS EVOLVED TYPICALLY FROM A SHORT PERIOD OF NON-WORK, AFTER A LONG TIME SPENT IN WORK WITH FEW FINANCIAL DECISIONS TO MAKE AT RETIREMENT, TO A MUCH LONGER PERIOD OF RETIREMENT WITH MORE DECISIONS TO BE MADE BOTH AT AND FOLLOWING RETIREMENT.

However, the changes the 2014 Budget announced, whilst challenging to implement and support, offer the opportunity of fitting retirement income much better to the way people actually retire as long as the right support is available to them.

- Pension changes – what has happened? What is freedom and choice? In a nutshell, all pension savers have been given the ability to access DC pension funds from the age of 55 with no constraints on how much can be taken, or when, other than those imposed by pension scheme rules and the support or otherwise of the employer. Subsequently, significant changes were announced to the 'death tax' regime to allow all unused DC pension savings to be passed to any beneficiary free of tax in some circumstances, thereby allowing for more sophisticated estate planning to be accessed by those same pension savers.
- Alongside these changes, new regulations were announced about the treatment of pension transfers for both DB and DC schemes; safeguarded benefits were identified as a trigger point for advice.
  - Regulated advice must be taken and evidenced before DB transfers valued in excess of £30,000 can be made.
  - DC pension pots with values in excess of £30,000 must also be checked for safeguarded benefits and where present, for example a built in guaranteed annuity rate, advice must be taken before access can be given.
- Pension Wise was launched – it is a free and impartial guidance service provided by the government, for DC scheme holders over the age of 50, delivered by The Pension Advisory Service and Citizens Advice Bureau. Its remit is to provide guidance on the retirement income options available to scheme members but to stop short of advice or recommending the most appropriate way forward for an individual.
- Longevity (life expectancy) – as the responsibility and risk inherent in providing an income throughout retirement transfers to employees/pension savers, the question of longevity i.e. living longer becomes an increasingly important one to understand.
- We might be familiar with the use of average life expectancies and the rapid increase of these, for example a man retiring at age 65 can expect to live for another 18 years and a woman for 21 years. However, what is often lost is the variability within these averages - retirement for many will be much longer. The graphic below adapted from the Money Advice Service highlights this. Yet the Pensions and Lifetime Savings Association's research found that only just over 1 in 10 thought their pension savings would have to last more than 30 years, rather than the 1 in 4 that will actually be affected.

Health and Longevity

People are living longer than they used to. A 65 year old man now has a 50% chance of living to 87 and a 65 year old woman has a 50% chance of living to 90.



A 65 YEAR OLD WOMAN HAS

75% chance of living to **82**
50% chance of living to **90**
25% chance of living to **96**
14% chance of living to **100**

A 65 YEAR OLD MAN HAS

75% chance of living to **79**
50% chance of living to **87**
25% chance of living to **94**
9% chance of living to **100**

Source: ONS Data, 2014

Research from the Pensions and Lifetime Savings Association and Club Vita has also shown life expectancy in DB pension schemes increasing by around two years from 2000 to 2010. Not only is this a liability issue for DB schemes but it signals to employees the need to plan for a much longer retirement.

The key message is; don't plan for an average, plan for something longer but be aware it could be a great deal shorter as well.

- An important effect created by increasing longevity and a long period of low interest rates has been the perception that annuities offer poor value as a retirement income vehicle. Annuity rates have been 'low' for a number of years, though the expected future rises in interest rates are likely to see some improvements in levels, and have been a key factor in the nature of the pension changes announced.
- Although rates are likely to rise in the future, there has been a significant fall in the numbers of annuities purchased in favour of pension savers embracing flexible drawdown. For some however, the nature of annuities means it will still be the best option for them.
- The decline of DB pensions is now well understood and while in 2000, 88% of private sector DB schemes were open to new members this had fallen to just 12% by 2013 with nearly one in three closed to future accrual.
- The Pensions Regulator's sixth annual statistical report on occupational trust based pension schemes highlighted that although more assets are still held within DB pension schemes, the number of DC savers has overtaken those in DB.
- This is no surprise. DC has been given a new lease of life with the successful introduction of auto-enrolment with over 5 million members enrolled in the first three years and an expectation that 9 million pensions savers will save for the first time or save more as a result.
- With hundreds of thousands of small and micro employers reaching their staging dates by 2018, the numbers of new savers who will need to understand the complex choices they face when using their pension savings is growing at an unrelenting pace.
- As a result of the likely skew from annuity to drawdown and encashment at retirement for DC members, some pension schemes are implementing a 'trident' approach to life-styling which may be 10 years, five years or three years from a selected retirement date. Rather than a single default fund being in place; which would take a pension saver from the age of 55 or so towards an annuity purchase at age 60 or 65 – schemes are offering options aimed at cash, annuity or remaining invested to access flexible drawdown. These are not simple decisions to make.
- The 'glide path'* choice is a new phenomenon and an important decision to be made by pension savers which could have a huge impact on the final amount of money available to produce their desired outcome. This issue alone presents a significant risk to pension savers and perhaps to schemes and employers as well.

* By glide path we mean how pension savings are invested in the years leading up to retirement.

- **Access and responsibility for use of DC funds lie with the saver.**
- **As longevity increases, many need an income for longer than anticipated.**
- **A secure income is valued but annuities are unpopular and DB is diminishing.**
- **Glide path choice should not be underestimated – there are risks for all.**
- **Advice must be taken in some circumstances.**

3
THE MARKET: RETIREMENT INCOME OPTIONS

WHAT ARE THE OPTIONS?

AS WE GO TO PRINT THERE ARE STILL THE SAME THREE MAIN OPTIONS AVAILABLE TO PENSION SAVERS CONSIDERING THE USE OF DC SAVINGS AS THERE WERE BEFORE THE PENSION CHANGES CAME INTO FORCE. THE DIFFERENCE IS THE FLEXIBLE OPTIONS ARE AVAILABLE TO MANY MORE SAVERS THAN PREVIOUSLY.

Broadly speaking these options are, buy an annuity, enter into some sort of income drawdown arrangement, take a cash payment to the value of the DC scheme, or indeed a combination of options.

However, the most important consideration is that these options do not and should not exist in isolation of each other, or other lifetime savings. Rather they are individual elements of a whole, complementary to each other when used to produce an income from a number of savings assets.

- **Annuity** – while sales of annuities have plunged since 2014, suggestions of the wholesale death of the annuity market in the face of the pension changes are arguably misplaced. For those seeking a secure and guaranteed income which addresses many of the risks that accompany the management of a flexible income; such as investment risk, longevity risk and inflation risk – an annuity is perhaps the only retirement income option vehicle that does this.

  Annuity rates are not static and may improve as interest rates rise. They allow for lifestyle and medical histories to be taken into account, so that an individual can receive an income from an annuity that is specific to their personal circumstances. The pension freedoms allow for income to be passed on to beneficiaries. In some circumstances this may be entirely free of tax.

  An annuity may form a valuable base to a considered plan to produce a lifetime income. The relative inflexibility of annuities remains and they are not risk free. However, without guidance and advice, pension savers may still make mistakes in the type of annuity they purchase which could see them subject to mortality risk for example - which is the loss of the value of pension savings through early death.

- **Income Drawdown** – in essence this is a flexible way to take retirement income, giving control over how and when an income is taken and providing an opportunity for capital growth to offset the effects of inflation. Instead of making a single one off decision to buy an annuity, income drawdown allows individuals to make a number of decisions to suit their changing circumstances in retirement, drawing an amount from their pension savings to be paid in much the same way as, for example, monthly like a salary or in tranches for specific needs.

AN ANNUITY MAY FORM A VALUABLE BASE TO A CONSIDERED PLAN TO PRODUCE A LIFETIME INCOME

It has flexible death benefits and in some cases the whole of the remaining fund can be left tax free to beneficiaries, so it may be seen as an effective tool when carrying out estate planning. As savings remain invested, effectively in the stock market, the capital value can fall as well as rise and this can have an effect on future income levels. It is this real risk that needs to be understood, in conjunction with the likelihood of a long life, particularly by those facing active decision making for the first time. The majority of workplace pension scheme members use default options when making decisions about where to put their pension savings. This is a strong feature of auto-enrolment, where no active decisions need to be made by scheme members in the joining and saving parts of membership. This is very different to the freedoms that the pension changes confer which introduce many pension savers to the concept of self-investment for the first time with its inherent risks.

Income drawdown, whether accessed as a one off or used to produce a flexible income, has the potential to allow pension savers to match the income they draw to the changing needs they have as they move from an active retirement through to one requiring more assistance and support, however it comes with risks.

- **Cash –** although a form of income drawdown, many will not see it as such. For those who want to manage the withdrawal of their pension savings as a cash sum only; either due to a low value or simply the desire to see their savings returned to them – the pension freedoms allow relatively easy access. Many schemes will facilitate the withdrawal of a cash sum, even the whole fund value, at the point of retirement. However, it is understandable that schemes will not want to take on the administrative and systems burden of managing a long term income drawdown relationship with what will be ex-employees, who are years into their retirement. Drawdown type facilities will be required by pension savers who want to mitigate tax liabilities when withdrawing cash sums from their savings, as all withdrawals are subject to marginal income tax rates once the standard 25% tax free allowance has been taken.

Whilst these options may have broadly remained the same, except for some important tax legislation changes introduced, they are not necessarily simple choices to make.

- There is the need to align retirement income options with the choices many in workplace pension schemes will need to make in the years preceding retirement.
- For example, buying an annuity or taking long term income from a pension fund via income drawdown is the culmination of the saving effort.
- The investment choices made prior to this have an important bearing on the value of the funds that will be available to do this. Investing in cash for 10 years before entering income drawdown is unlikely to make sense, nor would investing heavily in equities up until the point of retirement if an annuity or cash is the preferred retirement option.
- Pensions and Lifetime Savings Association research in March 2015 showed that nearly half of all pension savers would wait until retirement to make decisions about how to use their money or in fact weren't sure at all.
  - While 5% said they would purchase an annuity and 4% said they would take cash, 24% were planning on using a combination of options.
  - Nearly a fifth were planning on drawing an income from an invested pot.
- The evidence here is clear, that people are planning on embracing the changes but there is good reason to provide support in the form of financial education well before this point.

- **The three main options available to pension savers considering the use of their DC savings remain the same as pre pension freedoms. Research shows that a combination approach will be popular.**
- **Pre-retirement investment choices will be a new challenge to pension savers.**

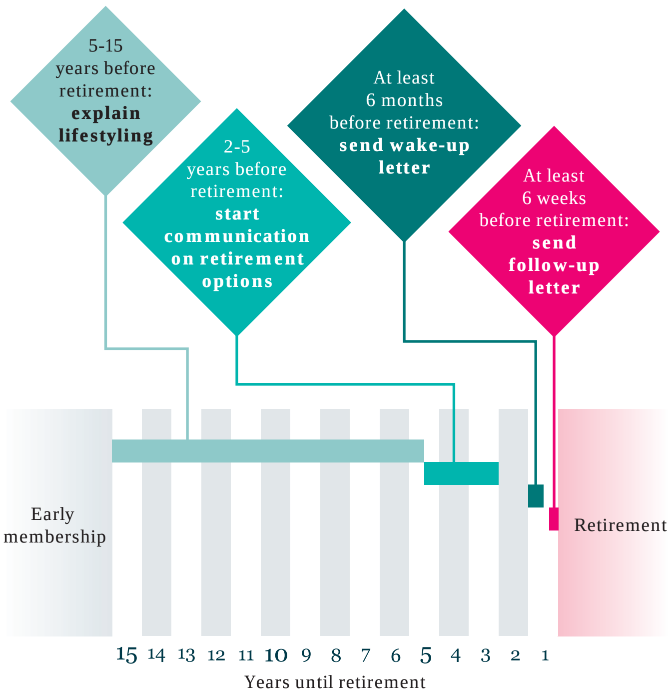
4 EMPLOYEES

EMPLOYEES: THE BACKGROUND

- In this brave new world of pension freedom and choice, it is possible that DC schemes and those that run and sponsor them can help deliver well thought out and planned retirement income outcomes for pension savers.
- They can do this by giving pension savers timely and comprehensive support ahead of any interaction with Pension Wise, so that by the time they do engage with them they have an understanding of the range of options they should consider.
- Historically, the take up of at-retirement support services from The Pensions Advisory Service and Money Advice Service appears to have been low down on the list of places pension savers seek help from. This was evidenced in research by The Association of British Insurers (ABI) when looking at the effectiveness of at-retirement communications and options for support.
- In March 2015, research commissioned by the Pensions and Lifetime Savings Association found that nearly a quarter of pension savers who were over the age of 55, had not heard of Pension Wise and that more than a third (35%) of those questioned said they were not likely to use it.
- Only months after the launch of Pension Wise, the government announced a change in the qualifying age to access the service from age 55 to 50 for DC scheme members.
- Given the disconnect between the scheme(s) members and a third party such as Pension Wise, it is important employers/trustees educate members long before retirement rather than relying on Pension Wise before or immediately at the point of accessing their DC pension savings.

WHAT SHOULD BE DONE?

- A framework for enabling good retirement decision making as proposed by The Pensions Regulator in November 2013 still holds well in our view despite the pension freedoms.
- That's because it recognised that a long lead in to the actual date of retirement was hugely important and that the process of educating pension savers is not a quick one.
- This should be the benchmark for all workplace schemes seeking to engage and support their pension savers.
- However, engagement isn't just about communication, in fact if it is only seen as a way of delivering more written words to savers then it is unlikely to succeed. Rather it should be about education first and the pension saver understanding that there is something in it for them, that it is worth knowing more and then carrying on that contact with one-to-one guidance and regulated advice where appropriate.
- The timeline below is an adaptation of The Pensions Regulator framework. It shows that early engagement and ongoing provision of financial education is a key process.



Enabling member retirement decisions
Retirement communications timeline

Over the last few years research based on behavioural economics show that in general DC members;

Don't:

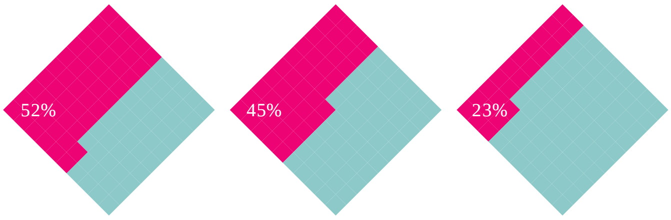
- really understand the implications of information given
- link short term decisions to long term consequences

Rather they:

- take the path of least resistance
- and 'under-think' complex decisions

HELPING PENSION SAVERS

- WEALTH at work's experience is that when provided with relevant information in person, pension savers act and in numbers. We would expect that at least 50% of those approaching retirement will seek one-to-one guidance and regulated advice following a financial education programme. This may be a surprising statistic but it demonstrates that how it is delivered is just as important as what is delivered.
- In the first tranche of the Pensions and Lifetime Savings Association's Understanding Retirement research programme, it was found that many pension savers saw the prospect of converting their pension savings into an income in both a positive and negative light. Many were pleased by the new freedoms but on the other hand were fearful that they did not have the capability to make the right decisions and that they will run out of money before they die, be mis-sold unsuitable retirement products, or simply make bad decisions.
- Almost three quarters of those expressing a preference on how they would access their DC savings said they would leave a proportion invested and draw a regular income.
- Unfortunately they did not have the full picture of what this might mean. The following diagram shows concerning statistics and demonstrates a lack of understanding:



Over half (52%) thought it would provide a guaranteed income.

45% thought their savings would last throughout retirement if they only matched an annuity income.

23% thought income drawdown was risk free.

Providing financial education and guidance before retirement should allow any pension saver to answer three key questions they may ask;

1. What do I need to know?

This is the keystone question. Individuals need to have a clear understanding of what options are available and the advantages and disadvantages of those options when taking into account, not just pensions assets (of which individuals may have more than one and of differing types e.g. DC and DB) but also other savings, investments and assets which may be used to generate income in retirement.

It should help shape thoughts on creating a retirement plan considering the cost of retirement, changing income levels and the impact of longevity i.e. how long they will need an income for. It will put the budget changes into context and help them understand how best to create their replacement income in retirement.

2. What is right for me?

Those approaching retirement will need support to work through what is the best personal decision for them, or indeed the first of what may be a series of decisions in the lead up to retirement and beyond. Assessing the full value of their assets available for retirement income and making decisions such as 'should I fully retire, delay my retirement or do I take a flexible approach to retirement?' should be at the heart of decision making.

Pension savers are different and will not want exactly the same from their retirement plan.

The answer to this question 'what is right for me?' is now highly personal and prompts further questions, such as;

- Should I access my pension now/later/ever?
- Should I take a lump sum/income or both?
- Do I want a secure income or will I take greater risk?

As they work out the likely best options, individuals will need to take into account specific issues around the types of pension savings they have.

For example, do they have a DC pension pot as a standalone savings fund? How can they access it and when? What are the taxes they're going to have pay when they take money out?

If, for example, an individual has deposit savings, general investments and pension funds and perhaps a property with a large equity value, how will they blend these assets together to create their 'personal income allowance' in the most tax efficient way?

Understanding the implications of different ‘shapes’ of retirement income should be a clear outcome for pension savers. For example, if they have a spouse, partner or any beneficiaries they want to pass money on to, it can be entirely free of tax in some circumstances and it’s important to understand that when thinking about ‘what is right for me?’

3. How do I implement it?

Once individuals have a good understanding of the options available to them and they know which are likely to serve them best, the last question to answer is all about action - whether that is some form of drawdown, annuity purchase, phased retirement or a combination of options which may change over time – just how do they go about doing it?

Again, there is no ‘one size fits all’ here for pension savers. Their actions will be determined by how confident they become through the education journey and how complicated their circumstances might be and for some there may be state benefit implications that may need to be taken into account.

If savers have a small DC pension pot from a previous employer they might simply draw cash from this in one go or over a couple of tax years. This could be done on a DIY basis directly from the scheme, or via a transfer to a low cost flexible pension provider.

However, if they have more complex financial needs and want to get an independent assessment of their options, then they can approach a regulated adviser and get firm recommendations; accepting that this is likely to be a paid for service.

There are a number of options available to pension savers at this stage, all of which can be provided through or by an introduction from an employer of the pension scheme.

Pension Wise – the impartial service provided by government and funded via the FCA levy must be signposted to members by DC pension schemes. This free source of information and guidance to pension savers should be on everyone’s list of places to seek help from. It can be accessed on a face to face basis, over the telephone or used purely for its online content and is available to DC members from the age of 50.

On a stand-alone basis it has obvious limitations, notably because it stops short of providing advice or making personal recommendations and doesn’t help those with DB pension savings. However, it does provide useful information about the retirement income options available and if no other support is available, it could help pension savers make better decisions.

Annuity broking – an annuity broking service can source a secure income which will be in place throughout retirement. It can be non-advised/DIY, advised as part of a limited or simplified advice service or wider financial planning service.

If offered on a non-advised basis, responsibility for the final decision made will rest with the pension saver and not the annuity broker; a case of buyer beware. Often commission costs will be the same or possibly more than an advised service and care must be taken to ensure the nature of the service is fully understood. Best practice is for a whole market approach to be taken and full medical and lifestyle underwriting to be offered. Anything less seems redundant in today’s retirement marketplace.

Robo advice – this term has been imported from the American investment market and is used to describe an online advisory service which gives recommendations based on an online fact find and an algorithm (rules based outcome). Usually focussed on a single product or transaction, it is relatively new to the UK retirement market and there are a limited number of services available.

DIY/Self-select services – these can be a mix of online only, or online services supported by telephone guidance where the pension saver can manage their own selected portfolio of investments, while drawing income to suit their needs. This service type is suited to those who are relatively financially sophisticated and have a good awareness of the various retirement income and other options available to them – as responsibility for decisions made lies wholly with the pension saver. Self Invested Personal Pensions (SIPPs) are available through some services allowing a pension saver to act as their own adviser. It should be noted that once the various costs involved are added up, for example, product fees, platform charges and dealing charges, these services can sometimes cost just as much as a regulated advisory service.

Regulated advice – means a recommendation to the pension saver which is presented as suitable based on a consideration of the person’s circumstances. It could be advice about a particular pension scheme or investment asset, or a broader planning based recommendation which can take account of the long term retirement aims and objectives of the saver. Typically this service will be fee based, offer regular reviews (at least annually) and will be able to provide advice on the full range of retirement options - annuity purchase, income drawdown, cash management or a combination of options. Planning based services should take account of all lifetime savings assets and be able to recommend a tax efficient strategy for creating a sustainable retirement income.

For pension savers who have a number of pension schemes, for example a mix of DB and DC arrangements, a specialist pension adviser with knowledge that includes pension transfers is likely to be required.

Regulated advice is usually available in the home, workplace or an adviser’s office and accessed by telephone or face to face.

Whichever option is chosen, it will be beneficial to receive guidance about the different types of support and advice available before accessing pensions and lifetime savings.

BRINGING IT ALL TOGETHER: BUILDING A RETIREMENT INCOME

To help employers, trustees and scheme members understand the complexities inherent in creating an income an example of combining the options available is shown here. The building blocks of this approach are not new but until the pension freedoms came into force, they were largely the preserve of those with significant levels of guaranteed retirement income or lifetime savings.

Is it as simple as it looks? Is it something all pension savers would feel capable of doing themselves?

The three main sources of income:

1. Taxable savings.
2. ISAs.
3. Pension savings.

EXAMPLE

The aim is to create an income of £12,000 per annum at age 60. Our pension saver has defined benefit scheme income available, cash in an ISA and DC pension savings.

Defined benefit – £6,000 pa

ISA – balance is £21,000

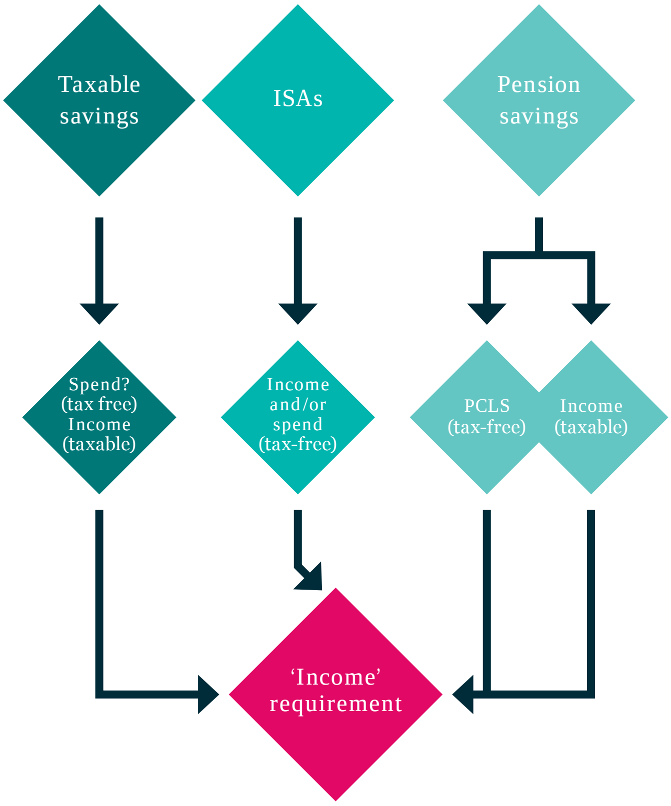
DC pension – balance £60,000

Using the 2015/16 personal allowance it is possible to generate this income in a number of ways without incurring any income tax.

The most appropriate way will depend on a number of personal factors relating to a pension saver's attitude to risk, capacity for loss, general retirement plans and a number of other considerations such as the age at which the state pension will be available.

In this example they could have simply taken the balance from the ISA until exhausted and then utilised the DC fund, or they could have purchased an annuity with the DC fund (around £2,500 pa after tax free cash) and used the tax free cash as an income top up for several years. Their aim should be to bridge the gap until receipt of State Pension.

Given the combinations available, the pension saver will need to consider the level of income needed, how long they need it for and the savings, investments and existing income available to contribute towards the target. This might sound obvious but in the past, employees simply bought an annuity with their pension pot rather than asking whether they actually needed the money. In the new pensions world this is likely to be the choice of the minority and flexing income or lump sum withdrawals from different sources to create a tax efficient income will hold sway.



- **Timing and engagement is important.**
- **Three key questions need to be answered.**
- **How bringing it altogether works in practice to build a retirement income.**

5
BEST PRACTICE – THE FINANCIAL EDUCATION PATHWAY

WE KNOW THAT PENSION SCHEME MEMBERS CAN STRUGGLE TO UNDERSTAND FINANCIAL INVESTMENT ISSUES AND OFTEN FAIL TO UNDERSTAND THE VARIOUS BENEFITS AVAILABLE TO THEM IN THE WORKPLACE. OF THESE, THE PENSION SCHEME IS TYPICALLY BY FAR THE MOST VALUABLE.

The reasons for this do not seem hard to find; the layers of jargon and complex terms that surround pensions and associated benefits, also a tendency to rely on passively delivered information, leaflets, booklets and content-heavy websites late in the retirement cycle and often only at the point of retirement itself.

The needs of all are different as are their learning styles. This is true also of sponsoring employers and trustees who must determine what support their budgets can facilitate.

It is worth understanding what we mean when we look at the different tools and interventions these interested parties can access in order to help scheme members answer the 3 fundamental questions of 'what do I need to know?', 'what options are suitable for me?' and 'how do I implement it?'

Prior to the pension changes announced in the 2014 Budget, The Pensions Regulator said;

"Changing working patterns, increases in longevity, low annuity rates and the availability of a greater range of retirement products mean that simply selecting a lifetime annuity at the state retirement age is by no means the only or best option. Trustees should ensure that members are made aware of the full range of options available to them, including commutation for small pots and members deferring their pension."

The pension changes have made this more relevant than ever.

FINANCIAL EDUCATION

Financial education is the facilitation of learning and the transference of knowledge and skills from one person to another. Financial education in this case refers to the understanding of workplace financial benefits and how they relate to an individual's broader financial circumstances. For example, how does a workplace pension relate to private savings and investments and how can they be used together to support a long lasting income in retirement?

There are a number of tools in the educators toolkit which can be used to reach today's diverse workforces; webinars and webcasts, animation clips, mobile phone apps, interactive games on websites and of course classroom based seminars.

An education programme tailored to a specific employer or pension scheme might be based on a three step approach including;

1. A review of existing employer benefits, understanding the strategic objectives of the employer/scheme and confirming the profile and demographics of the workforce.
2. Identification of hot spots/weak points and areas of greatest added value for scheme members.
3. A programme structure tailored to budget, location and the workplace benefits available e.g. the pension scheme(s).

Typically financial education is not a regulated activity and is not specific to any one individual, rather aiming to provide general direction and information to a wide range of scheme members and employees.

Group size is important. An optimum number of attendees being 16-20 encourages participation without spotlighting individuals whose learning style is to listen and absorb, while allowing those who prefer a more interactive style of learning to do so at the same time.

As part of an education pathway to retirement we suggest it would be good practice to start this programme at least 10 years before normal retirement dates kick in; this is in line with The Pensions Regulator's guidance.

The Pensions Regulator recognises the decisions that members will need to take in order to optimise income at retirement begin a number of years before retirement and certainly no later than the start of life-styling choices, or de-risking of target maturity funds. With the introduction of freedom and choice in pensions, 10 years ahead of retirement may be the minimum point that this should start, as a number of schemes will expect glide path/ life-styling selections to be made then.

Increasingly this timeframe will expand and 45 will become a more appropriate age at which to start to deliver financial education on retirement options. This is driven by the ability to access DC pension assets from the age of 55, which at present is in place until 2028, and requires careful consideration of investment options if a scheme member is planning on early access.

Guidance can be sourced on a tailored basis by sponsoring employers or trustees. In addition the government backed Pension Wise service can be accessed for guidance for anyone aged 50 or over in respect of their DC pension.

A typical session may be conducted face to face, in the workplace or over the telephone or skype.

TAILORED PROGRAMMES OF ONE TO ONE GUIDANCE CAN ADDRESS SPECIFIC EMPLOYER AND SCHEME ISSUES

GUIDANCE

Again this is not a regulated activity as such but it is likely to be with a financial professional who can help scheme members/employees clarify elements of their financial situation and even lay the groundwork for an ongoing financial plan.

While guidance specifically falls short of providing a personal recommendation in relation to pensions and other lifetime savings and investments, it is extremely useful for helping members understand personal options in more detail and in a private setting. So, it can tell you what you can do, but not what you should do, although it can signpost to regulated advice and inform about how to get advice and where different types of advisory services are available.

Tailored programmes of one to one guidance can address specific employer and scheme issues such as those raised by the Lifetime Allowance or scheme liability management programmes such as a Pension Increase Exchange offer.

Although advice is not given it is best practice to supply a written summary of the meeting.

Pension Wise offers web information in support of guidance sessions carried out over the telephone or in a face to face setting.

The guidance is free and impartial, refraining from recommending either a specific course of action or making an introduction to a specific advisory firm. This was an important point in the set-up of the service, ensuring there was no financial relationship with commercial entities. Appointments may require some preparation to be made. It is a requirement that trustees and the administrators of contract based schemes clearly and effectively signpost members to Pension Wise.

A possible drawback with Pension Wise is the timing of the intervention as it is likely to come at the point of access to pension savings or retirement itself, rather than laying the early groundwork for engagement and understanding, despite being accessible from age 50 for DC members. And for DB only pension scheme members, Pension Wise is not available at all.

Ideally, Pension Wise would be a fine tuning or sense check for all scheme members complementing a tailored financial education programme, rather than the only point of contact to discuss retirement options.

ADVICE

Regulated advice is a natural next step for many following a structured financial education programme.

For many, obtaining financial advice tailored to their particular circumstances will make sense.

The pension and retirement landscape has become more complex with the advent of freedom and choice; there are more issues for individuals to deal with and with the end of compulsory annuitisation, there is a likelihood that many more will enter into some form of flexible drawdown with all the attendant transference of risks from the scheme/insurer to the member that entails.

As schemes and trustees communicate with members about the need to engage with Pension Wise and highlight the key risks members face in accessing and utilising their pension savings, it is recognised by The Pensions Regulator that this may trigger a requirement to engage with an authorised adviser. They say that,

“If, having been provided with the generic risk warnings, a member asks further questions about their retirement options be prepared to direct them toward Pension Wise for further guidance and/or an FCA-regulated financial adviser for advice specific to their personal circumstances and their selected retirement option”.

There is no regulatory requirement for employers or trustees to appoint authorised advisers to support members with their retirement income decisions. However for any scheme that wishes to do so, it should follow a due diligence process to ensure the advisers in question enjoy financial stability and have the requisite resource capabilities and experience to be able to deliver a consistent service to the member group in question.

Updated regulation about pension transfers and the introduction of safeguarded pension benefits have highlighted the need to engage advisers with specific at-retirement and pension knowledge rather than generalists.

- **Best practise provides financial education at least 10 years before retirement.**
- **Tailored programmes of one to one guidance can address specific employer and scheme issues.**
- **Advice can often help with complex investment or tax considerations.**

6 CONCLUSION

There is no doubt that for the upcoming generations of pension savers, there are more opportunities to shape a retirement income that has the potential to meet what will be their changing needs and priorities throughout their retirement. The ability to access DC pension savings from the age of 55 may see 'retirement', if that term is used to define the period of access to specific retirement savings, actually spanning 40 years or more and with all of that comes greater risks.

As time goes by the lines between general savings, savings for a car or a mortgage and savings for retirement may blur and be considered as just an element of their lifetime savings. However, while valuable tax benefits and financial planning opportunities remain around pensions savings, and while there are significant differences between the secure pension provision of DB schemes and the new laissez faire accessible DC schemes, it is important now more than ever for employers and pension schemes to provide professional guidance and support to pension savers.

There is a lot of common agreement that more financial education is needed to support pension savers. Each year WEALTH at work carry out a survey of HR, Reward and Pension professionals to capture their views on the retirement income scene.

Over the years, results have been pretty consistent. Last year for instance, 88% of those surveyed thought professional retirement planning including financial education was really important but 57% didn't think or didn't know if their employees would know where to go to get advice.

This is a concern because 58% did not think their employees knew what retirement income options solutions were available, or knew the pros and cons of the various options.

Pension savers face more risks now if going it alone or entering unchartered territory with their retirement income decision making, but as this guide highlights, there are a number of things that can be done to help them improve the outcomes they will get; most notably by providing access to financial education, guidance and advisory services.

Like an individual retirement plan, there may not be a 'one size fits all' answer for employers or scheme trustees seeking to provide more support to members. There are professional services available that can provide tailored support alongside or independent of the scheme, that will support a pension saver throughout their membership ranging from classroom based financial education, to online planners and modellers, one to one guidance and on to regulated financial advice and planning.

These can be accessed via existing scheme administrators, Employee Benefit Consultants, or from specialist financial education providers.

Sourcing these services requires an understanding of what is on offer and the due diligence an employer or trustee group will undertake may not differ markedly from the sourcing of a pension scheme administrator or investment manager.

Financial education

- Is the provider an expert in the area of financial education?
- Can they provide a scalable and tailored programme aimed at different age and career stage membership groups?
- Can they offer project and event management support?

Guidance

- Can they support members on a one to one basis?
- Do they offer face to face, phone or web based support?
- Can the guidance cover a range of scheme specific issues?

Advice

- Are all advisers authorised and registered with the regulator?
- Is retirement a specialist area?
- Are fees transparent and fair?

Before selecting a provider of financial education services, it is good practice to attend existing education and guidance programmes to check delivery quality and always take references from existing employers or schemes already using the services.

Build in regular reviews and ensure that robust management information is available to gauge value added to the scheme, employer and member of any of the interventions that are delivered.

Finally, once a provider has been selected, make sure there is a contract in place for the required services that allows a full review periodically.

NOTES

DISCLAIMER

Please note, at the time of writing this guide The Pension Regulator was consulting on potential changes to The DC Code and Guidance to be released in 2016. Therefore, the content in this guide is subject to change dependent on the findings.

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