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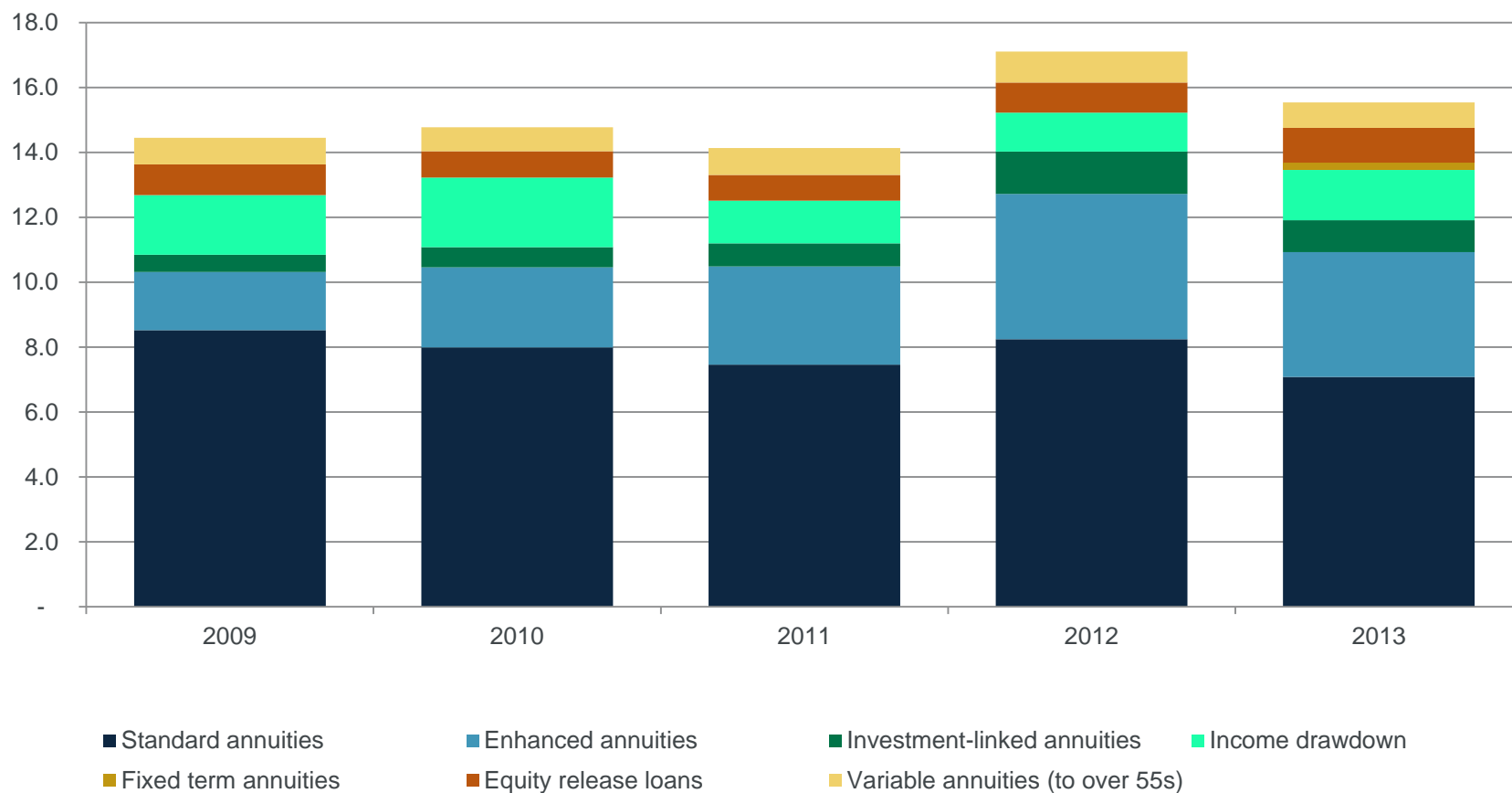
What a Budget! Implications for the At-Retirement Market

Bernie Hickman, Legal & General
Kamran Foroughi & Michael Armitage, Towers Watson



Retirement market was already evolving

Chart shows premiums and equity release loans per annum (£bn)



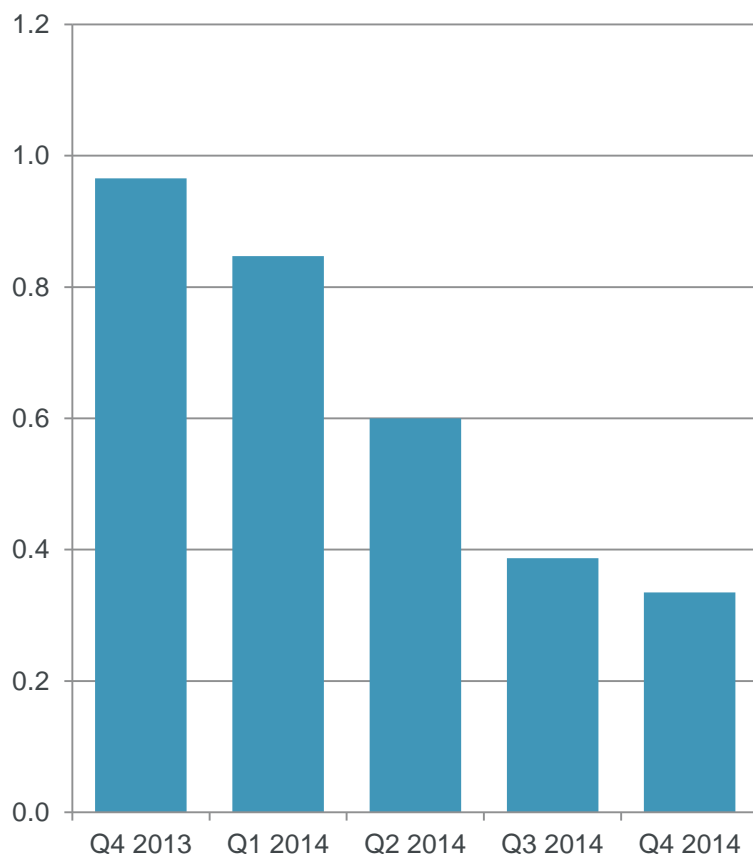
Source: Towers Watson analysis of ERC and ABI data (includes ABI members only) and Towers Watson variable annuity and enhanced annuity surveys.

Budget announcement introduced greater flexibility

- From April 2015
 - DC pots can be withdrawn from age 55 subject to marginal rate of income tax (after lump sum)
 - DC pension holders to receive free and impartial guidance on retirement options
 - Minimum age to access pension pot will increase to 57 in 2028 and rise with the state pension afterwards
- Government consultation on changes including
 - Guidance
 - Whether (funded) DB to DC transfers should continue
- Interim measures until April 2015 - Drawdown limits relaxed and easier to take small pots as lump sums

Recent impacts on retirement market

Enhanced annuity premiums per quarter (£bn)



Source: Towers Watson enhanced annuity survey, Press Release February 20, 2015

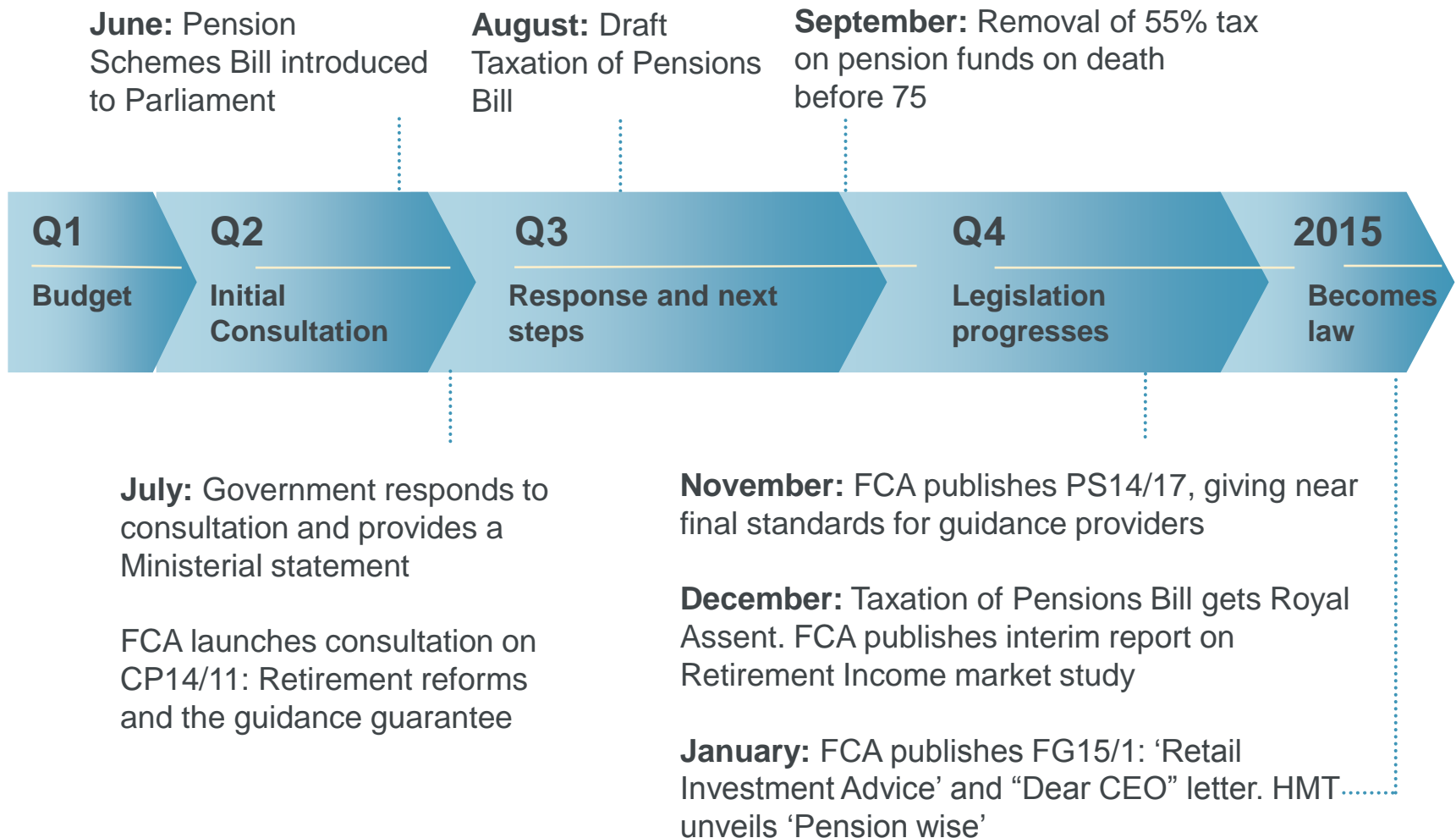
Standard Life UK annuity sales down **67%** in Q3 2014 relative to Q3 2013

*Q3 Interim Management Statement
29 October 2014*

The number of drawdown contracts sold by ABI members more than doubled compared to Q4 2013, with a reduced average pot size

ABI Press release
26 February 2015

Subsequent key developments



What about guidance?



Design



Deliver

**The PENSIONS
Advisory Service**



Engage








Education

Guidance

Advice

Selected overseas retirement markets

				 
Workplace retirement savings	Voluntary	Mandatory	Voluntary	Mandatory
Implicit default	Withdrawal	Withdrawal	Semi-active choice	
Proportion taking annuities	<10%	<10%	66% medium pots	70%-80%

What factors will affect the UK market?

Government

State benefits

Default
option

Culture

“ Good
value ,”

Customer engagement

Guarantees

Pre-retirement decisions affect post-retirement outcomes

Base assumptions:

- Individual saves from 25 and retires at 65
- 5% contribution rates at all years
- Starting salary £20k, salary inflation 2%
- 3% pa investment return

Scenario	Pot size at retirement	Versus Base (%)
Base	£114k	
1. Start 10 years later	£82k	(28)%
2. As Base, increase contributions to 8% at 35	£163k	+42%
3. As 2, increase contributions to 11% at 45	£195k	+71%
4. As Base, investment returns up to 4%	£143k	+25%

Auto-enrolment gets more people saving

85-90%

enrolled to date

7m in 5 yrs

new savers

Minimum contributions increasing

2%
now

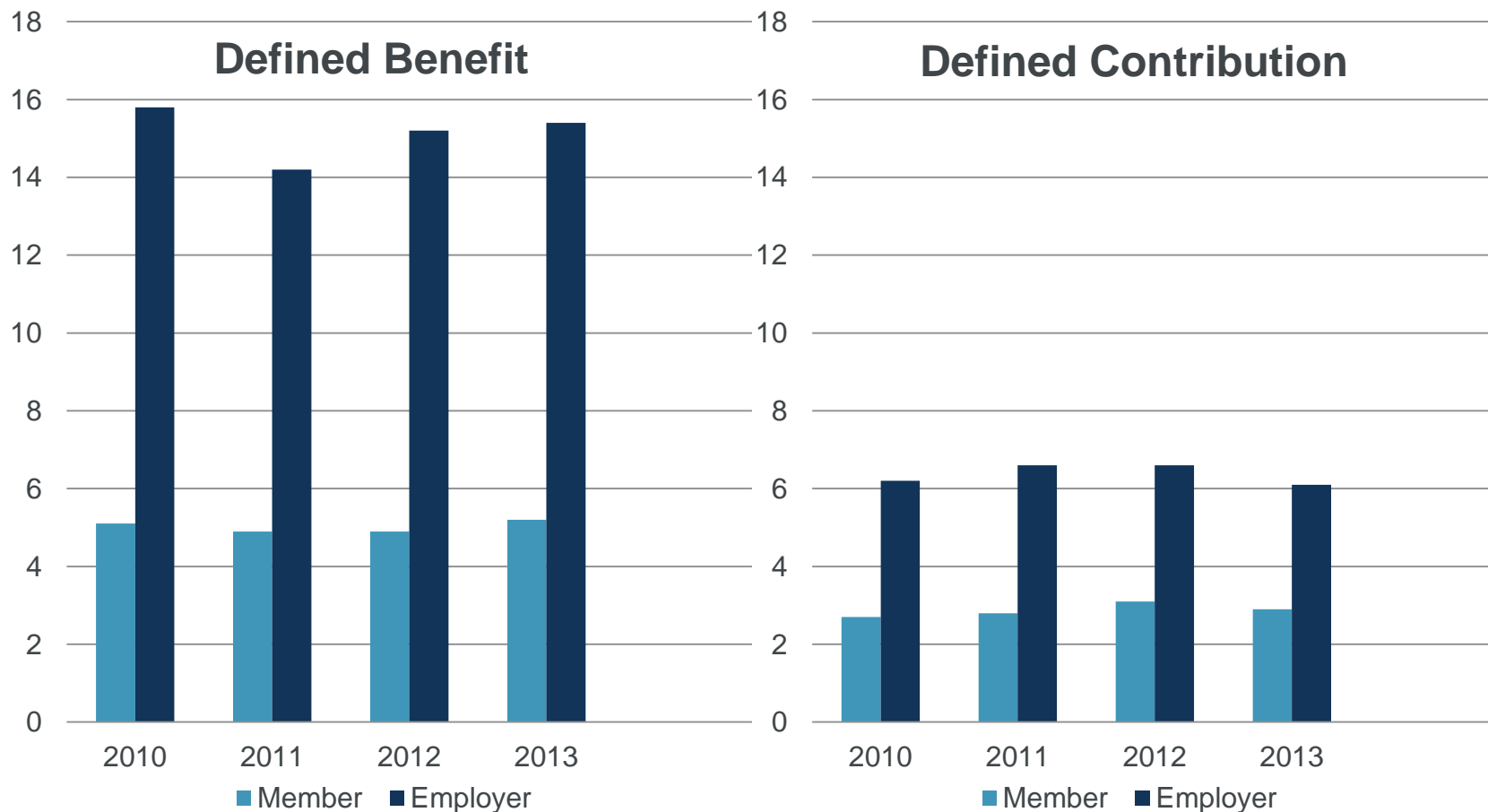
5%
2017

8%
2018 +

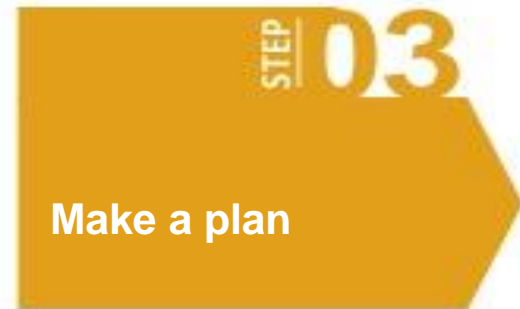
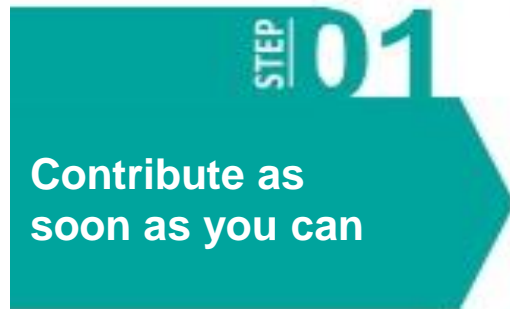
Sources: *Pensions Policy Institute automatic enrolment report (July 2014);
DWP automatic enrolment opt out rates report (November 2014)*

Contribution rates to private sector pension schemes (%)

Source: 2013 Occupational Pension Scheme Survey, ONS



Keeping customer engagement simple

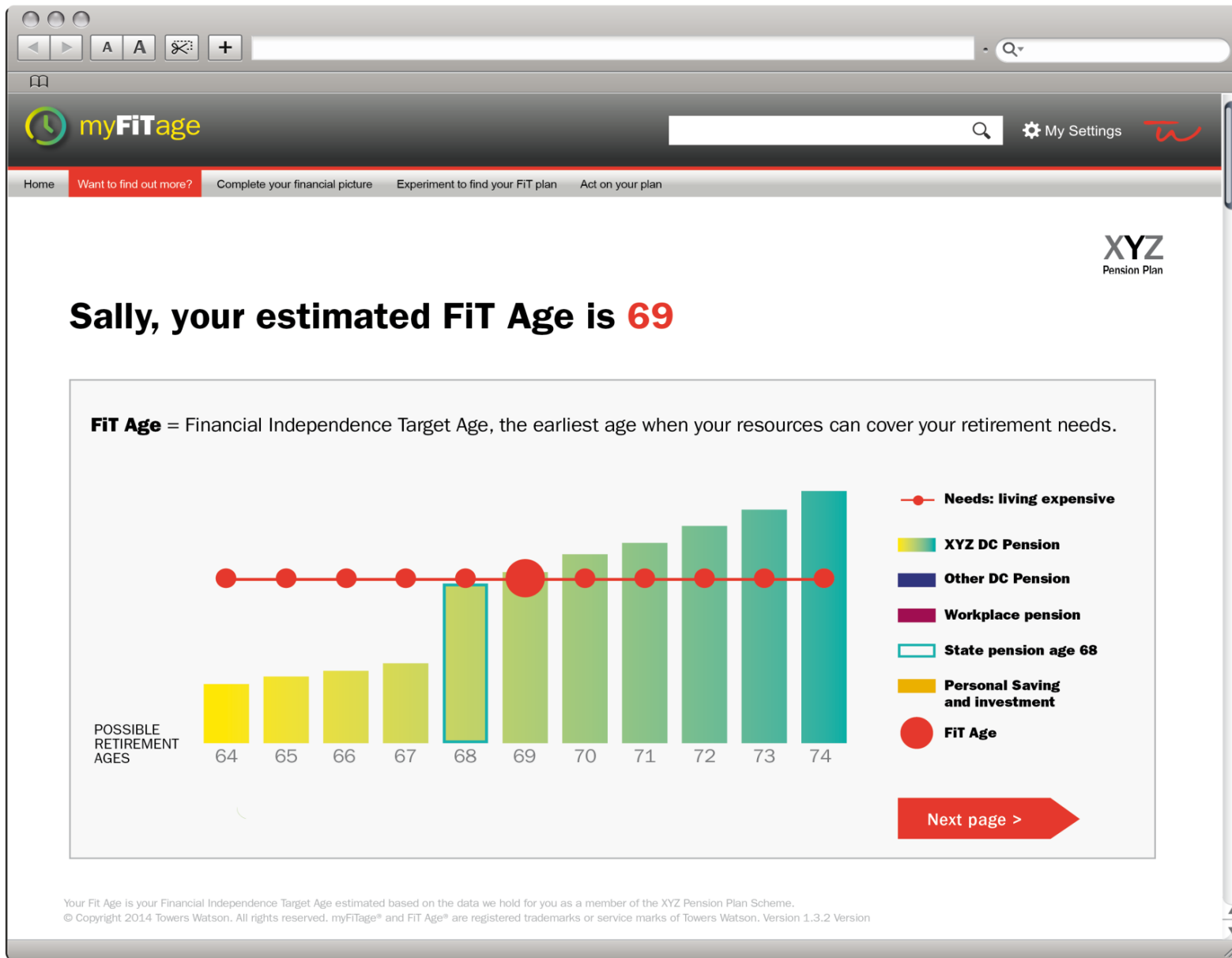


Effective communication

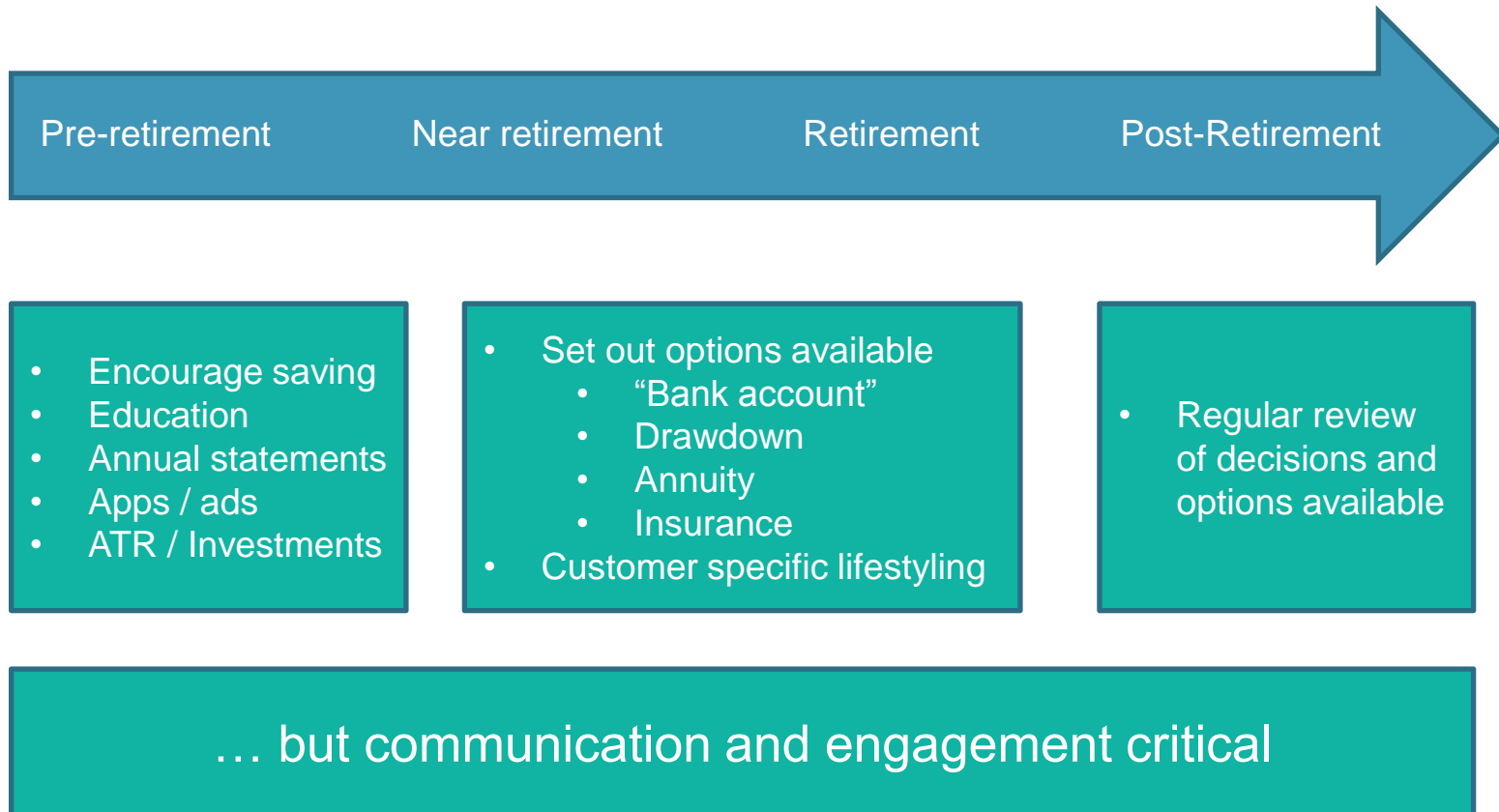
FiT Age = Financial Independence Target Age

the age at which an employee's total saving resources are expected to meet retirement needs.

An approach to addressing benefit adequacy issues



We have the building blocks for a successful future ...



What a Budget!

Implications for the At Retirement Market.

WE KNOW **EVERY DAY MATTERS**
AND WE NEVER FORGET **OUR SOCIAL**
PURPOSE WHICH SEES OUR DEDICATED
PROFESSIONALS
COMMITTED TO BRINGING **FINANCIAL SECURITY**
TO **OUR CUSTOMERS**, FROM
FIRST TO LAST TIME BUYERS,
FROM THE WORLD'S LARGEST
PENSION FUNDS TO THOSE ON A
DEADLINE TO THE **BREADLINE**,
WE DELIVER **SOCIALLY USEFUL**
PRODUCTS AND PROVIDE **VALUE**
TO **OUR CUSTOMERS.**

**EVERY
DAY
MATTERS.**

Bernie Hickman
Managing Director,
Legal & General Individual Retirement



RESPONDING TO REGULATORY SHOCKS.

“NO ONE WILL HAVE TO BUY AN ANNUITY”

George Osborne, 19th March 2014

**“YOU CAN’T PASS ON TO THE NEXT GENERATION ANY OF YOUR PENSION POT WHEN YOU DIE,
WITHOUT PAYING A PUNITIVE 55% OF IT IN TAX...I CHOOSE TO ABOLISH IT”**

George Osborne, 29th September 2014

What should customers do now at retirement?

Which customers now need a lifetime income from their Pension savings?

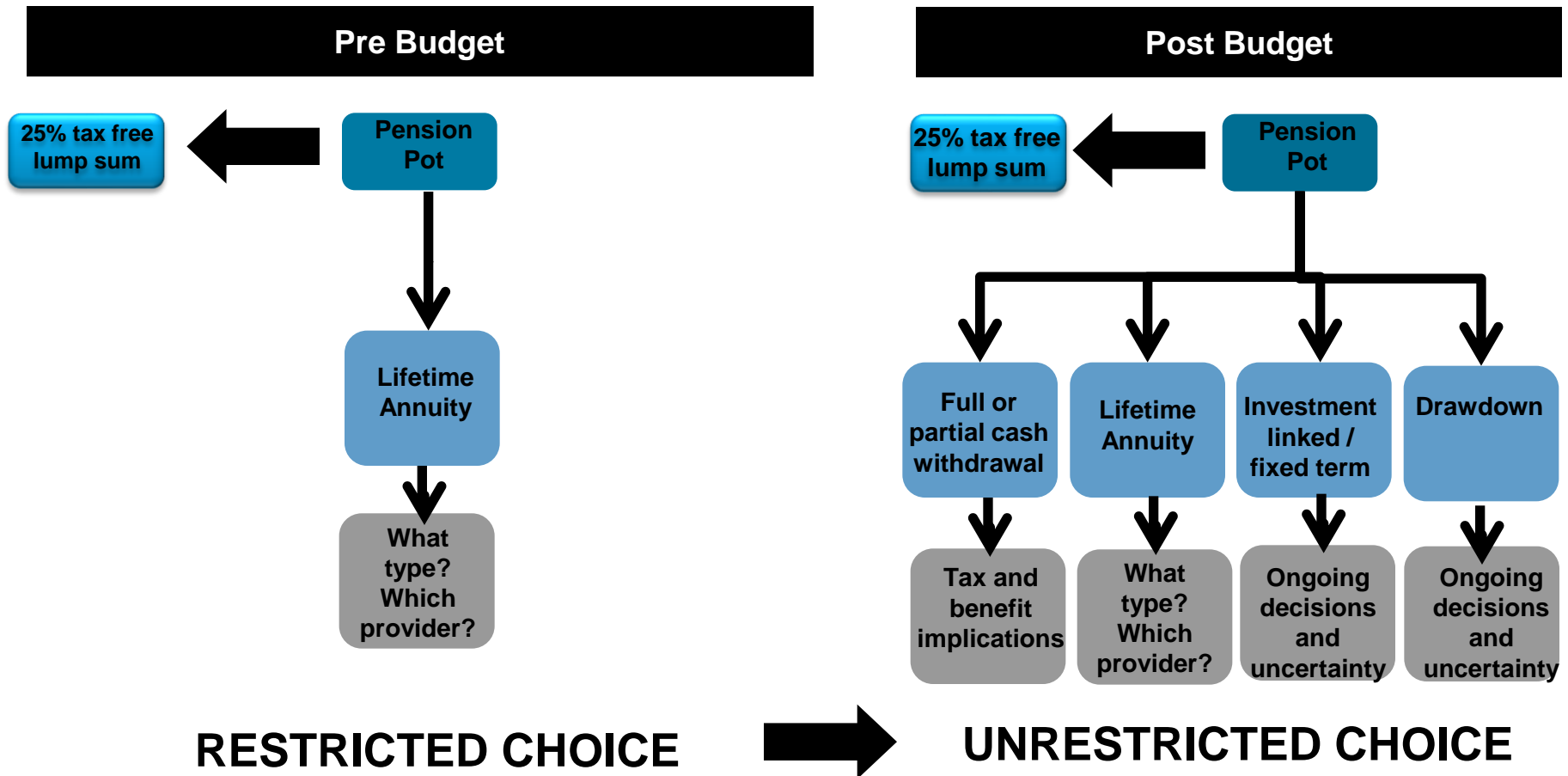
What challenges and issues do these changes present for the industry?

“Giving people the freedom to choose whether or not to buy an annuity is rather like being invited to jump out of an aircraft at 30,000 feet and being told that you now have the freedom to choose whether or not to use a parachute. Choosing not to annuitise is fundamentally no different from choosing not to wear a parachute.” Source (slightly paraphrased): The consequences of not having to buy an annuity, Dr David Blake, Professor of Pension Economics at Cass Business School

CHOICE BRINGS COMPLEXITY.

We love the idea of choice but often hate choosing

Practical reality for mass market customers:



WHAT DOES IT REALLY MEAN FOR CUSTOMERS?

1. WANTS CASH, LOW NET SAVINGS

“ I took all of my pension in cash over a few years and my benefits were protected”

John was a caretaker, earning below the national average wage. John had enrolled in his employers' pension schemes where he has pension savings of £16,000, but had no other savings. He lives alone in a rented 1 bed flat and receives housing benefit, council tax support and Pension credit. He has no family.

Retirement age

65

DC pension pot

£16,000

Other savings

£0

State pension

£7,714

Other income

£0

State benefits

£9,840 p.a.

Options	Retirement Income	Tax liability	Impact on benefits	Net of tax value	
1. Lifetime Annuity The income from the annuity counts against his benefit entitlement.	£4,000 TFC and £840 p.a.	- £0	- £562p.a.	= £7,971	✗
2. Flexi-Access/4 year income The income from Flexi access drawdown reduces benefit entitlement for 4 years	£4,000 TFC and £3,065 for 4 years	- £0	- £2,073 for 4 years	= £7,967	✗
3. Take all the Cash Only £10,600 is paid straight away as the emergency tax rate is used. Tax forms needed to reclaim the extra tax.	£16,000	- £1,943	- £0	= £14,057	✗
4. Partial Lump Sums Taken over 4 years to ensure no income tax paid	£4,000* for 4 yrs	- £0	- £0	= £16,000*	✓

*plus tax free investment returns

2. MODERATE NET SAVINGS AND GOOD INCOME

“ I took cash from my pension to boost my savings and pay for several holidays”

Simon has worked for a bank for the majority of his career. He has no family to support. His DB and State pensions provide him with enough to live on, and he wants to use his DC pot for holidays and other luxuries, but without straying into the 40% tax band.

Retirement age 65	State pension £5,881
DC pension pot £30,000	Other income £19,000 p.a.
Other savings -£5,000 (mortgage)	Property value £180,000

Options	Retirement Income	Tax liability	Net of tax value	
1. Lifetime Annuity	£7,500 TFC and £1,293 p.a.	- £259 p.a.	= £25,493	✗
2. Flexi-Access Drawdown Withdrawals kept below personal allowance level. Ongoing decisions and investment risk. Charges will reduce investment returns.	£7,500 TFC and £22,500*	- £4,500*	= £25,500*	✗
*plus/minus investment return less charges				
3. Guaranteed Income for 5 years Simple and tax efficient. No investment return upside or downside.	£7,500 TFC and £4,800 for 5 years	- £960 p.a. for 5 years	= £26,700 over 5 years	✓

3. WANTS REGULAR INCOME, MODERATE NET SAVINGS

“ I used my pension to provide me with peace of mind and a regular income”

Amy was the manager of a privately owned nursery. She has built up a decent DC pot but has no other retirement income except the State pension. Her husband Steve is a kitchen fitter and has no pension savings. They own their house outright, have a modest amount in a cash ISA and have no appetite for investment risk

Retirement age

63

DC pension pot

£80,000

Other savings

£20,000

State pension

£5,881

Other income

£0

Property value

£280,000

Options

1. Lifetime Annuity

To afford a more active retirement they will need to downsize and/or take out a lifetime mortgage. State support will be needed to fund care.

Retirement Income

£20,000
TFC and
£3,053
p.a.

Tax liability

£0

Net of tax value

£80,000
(over 20
years)

✗

2. Flexi-Access Drawdown

Withdrawals kept below personal allowance level. She will need to continually make decisions on how much to take out, funds to invest etc. She is exposed to investment risk. Charges will reduce investment returns.

£20,000
TFC and
£60,000*

£0

£80,000*

✗

*(plus investment returns less charges)

3. Guaranteed Income for 20 years

Simple. No income after 83. State will need to fund all care costs plus other eligible means tested benefits.

£20,000
TFC £4,600
p.a. (for 20
years)

£96

£111,904
(over 20
years)

✓

4. HIGH NET SAVINGS, IHT WORRIES

“ I used my pension fund to reduce the potential inheritance tax bill if I passed away”

Rachel has her own business. Her husband died 6 months ago. She is keen that her 2 sons inherit as much as possible on her death, but is worried about inheritance tax. The mortgage was paid off when her husband died so has no debt. She is risk adverse.

Retirement age

63

DC pension pot

£430,000

Other savings

£240,000

State pension

£5,881

Other income

£0

Property value

£650,000

Options	Retirement Income	Tax liability	Net of tax total	
1. Lifetime inflation linked Annuity with 30 year guaranteed payout	£107,500 TFC and £9,369 p.a. (plus inflation)	- £1,050 p.a.	= Depends on inflation	x
2. Flexi-Access Drawdown Uses other savings and releases housing equity leaving funds untouched. Good IHT mitigation but exposed to investment risk.	State pension, TFC plus other savings	- minimal	= Depends on investment performance	x
3. Guaranteed Lump Sum in 12 years No inheritance tax in the event of death before age 75. She could use her savings to fund living expenses for the next 12 years.	State pension, TFC plus other savings	- minimal	= £562,500	✓

5. Guaranteed Annuity option HIGH NET SAVINGS

“ My pension product gave me a pension annuity far higher than I can get on the open market”

Anne has her own business and is single. She has no close relatives so wants to provide herself a financially comfortable retirement. She is risk adverse and keen to secure a guaranteed income to meet her living needs.

Retirement age

63

DC pension pot

£430,000

Other savings

£500,000

State pension

£5,881

Other income

£0

Property value

£500,000

Options	Retirement Income	Tax liability	Net of tax total	
1. Lifetime Annuity using GAO	£107,500 TFC and £22,500 p.a.	- £3,500 p.a.	= £677,500 over estimated 30 years	✓
2. Flexi-Access Drawdown	All sources	- Depends on drawdown rate	= Depends on investment returns	✗
3. Guaranteed Lump Sum in 10 years	State pension plus other savings	- minimal	= £582,500	✗

BUDGET CHANGES = MORE CHOICE = MORE COMPLEXITY.

PERSONAL BALANCE SHEET

Size of pension pot



Other income



Capital e.g. homeowner



Debt



State Benefits



OTHER CONSIDERATIONS

Dependents



Desire to leave inheritance



Health



Standard of Living



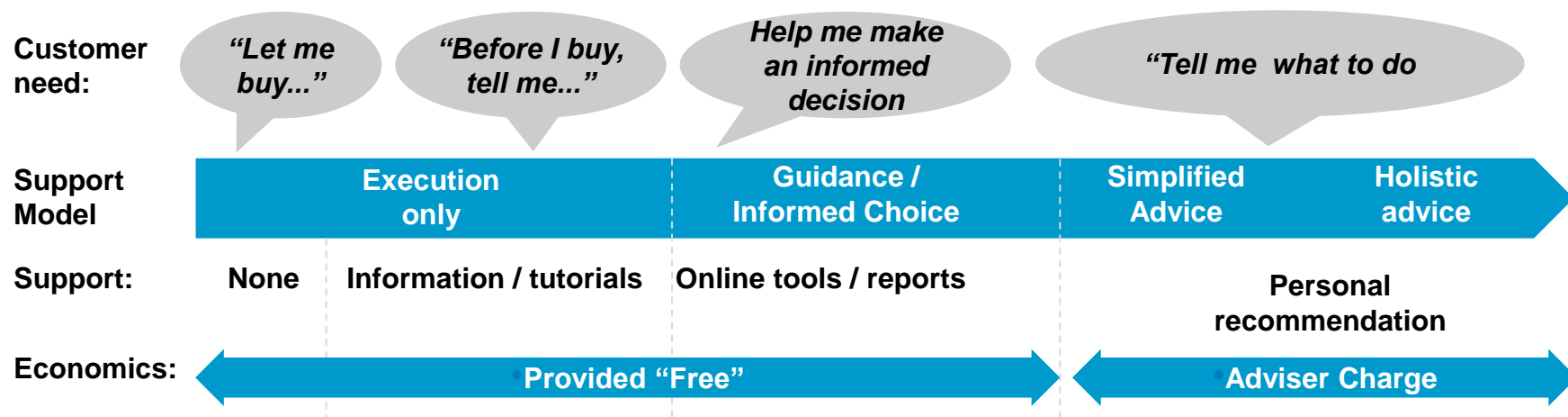
Investment expectations



Other things to think about:

- Deferring State pension
- Continuing to make pension contributions until age 75

CUSTOMER ENGAGEMENT CHALLENGE.



MARKET INNOVATION
e.g. mix of phone & web

FCA EXPECTATIONS
GC 14/3 recognises need to stimulate innovation to address mass market need for advice

CUSTOMER NEED FOR ADVICE IS CLEAR
MASS MARKET SOLUTION IS NOT CLEAR

NO REGULATORY DISTINCTION BETWEEN SIMPLIFIED ADVICE AND HOLISTIC ADVICE

NEW DIGITAL ENGAGEMENT FROM L&G

Educational Content

Pension Wise /
Advice

The basics

What you need
to know

What are my
options

L&G Products

Case study selector

You're done!

You've told us you're interested in...

Defined contribution pension less than **£30,000**

Other income less than **£15,000 to £30,000**

Non-pension savings less than **£40,000**

Examples of **Homeowners**

The case studies below reflect your answers to the questions asked.

Click through the different examples to see different retirement income options.



CHRISTINE
Took pension as
a lump sum.



NICK
Left his pension
invested.



PAULA
Took pension as
a lump sum.



DEREK
Accessed his
pension flexibly.



PETER
Used pension to
provide income.

Navigate Case Studies [◀](#) [▶](#)

Retirement Income Calculator

About You

Age

65

Postcode

BN3 1SE

What pension savings do you have?

£ 40,000

How long would you like to receive a retirement income for?

☐ The rest of your life ☒ A fixed term

Do you want to receive a lump sum payment at the end of the term?

☐ Yes ☒ No

Number of years you want to receive income

10

OR What income would you like?

You only need to answer one of these questions - choose the one you find easiest to answer.

Calculate

Income Estimate

Based on this information we will pay you a yearly income of **£ 4,400** a year for **10 years**, less any income tax you need to pay, with no lump



travel

Advice *Reviews* Inspiration *Expertise* Offers



Telegraph Tours
See the 'real' Marigold Hotel

Some like it hot
10 great volcano tours

Cruise Style
Special 24-page supplement

The Daily Telegraph



20

...well maybe not all of it. But with new pension reforms soon to come into force, Telegraph Travel has some great ideas about what to do with a financial windfall



WAYS TO SPEND THE KIDS' INHERITANCE



NEW AT-RETIREMENT MARKET.

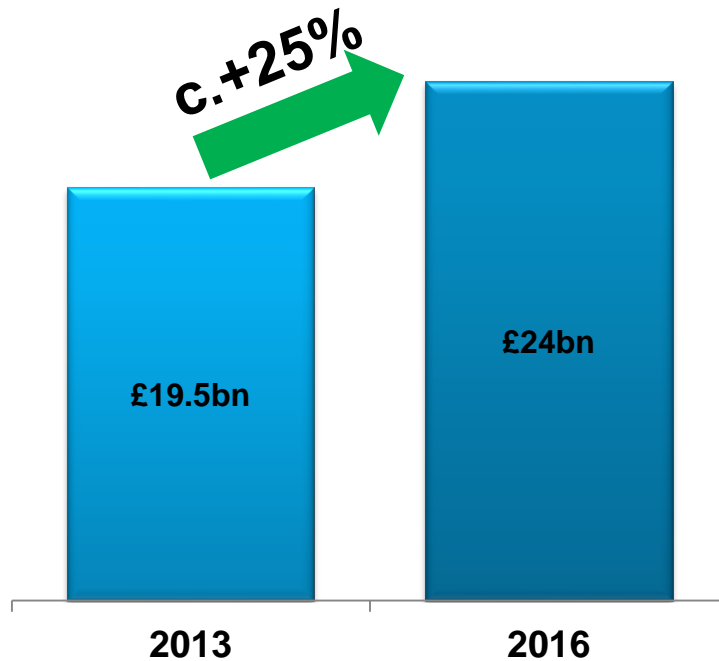
			2015 Estimates		
Customer pot size	2013 Market premium (£bn)	2013 Market Count (000's)	Cash/Savings	Lifetime Annuities	Drawdown/New Product
<10k	0.5	101	0.4	0.1	0.0
10k – 30k	2.2	122	1.4	0.4	0.4
30k – 80k	4.2	92	2.1	0.8	1.3
>80k	5.0	38	1.0	1.5	2.5
Total	11.9	353	4.9	2.8	4.2
		Existing Drawdown			1.6

BEYOND APRIL 2015.

THE INDIVIDUAL RETIREMENT MARKET WILL CONTINUE TO GROW -
THE PROFIT POOL WILL SUBSTANTIALLY REDUCE.

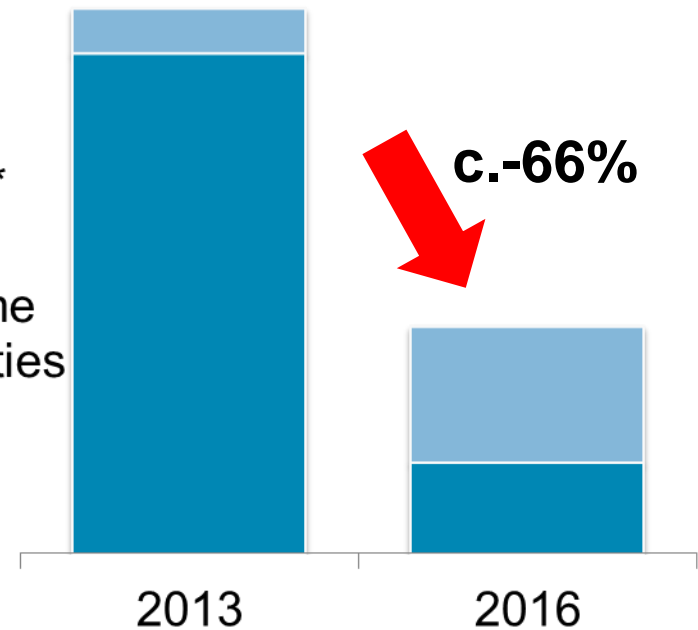
MARKET SIZE

PROFIT POOL **



■ Other*

■ Lifetime Annuities

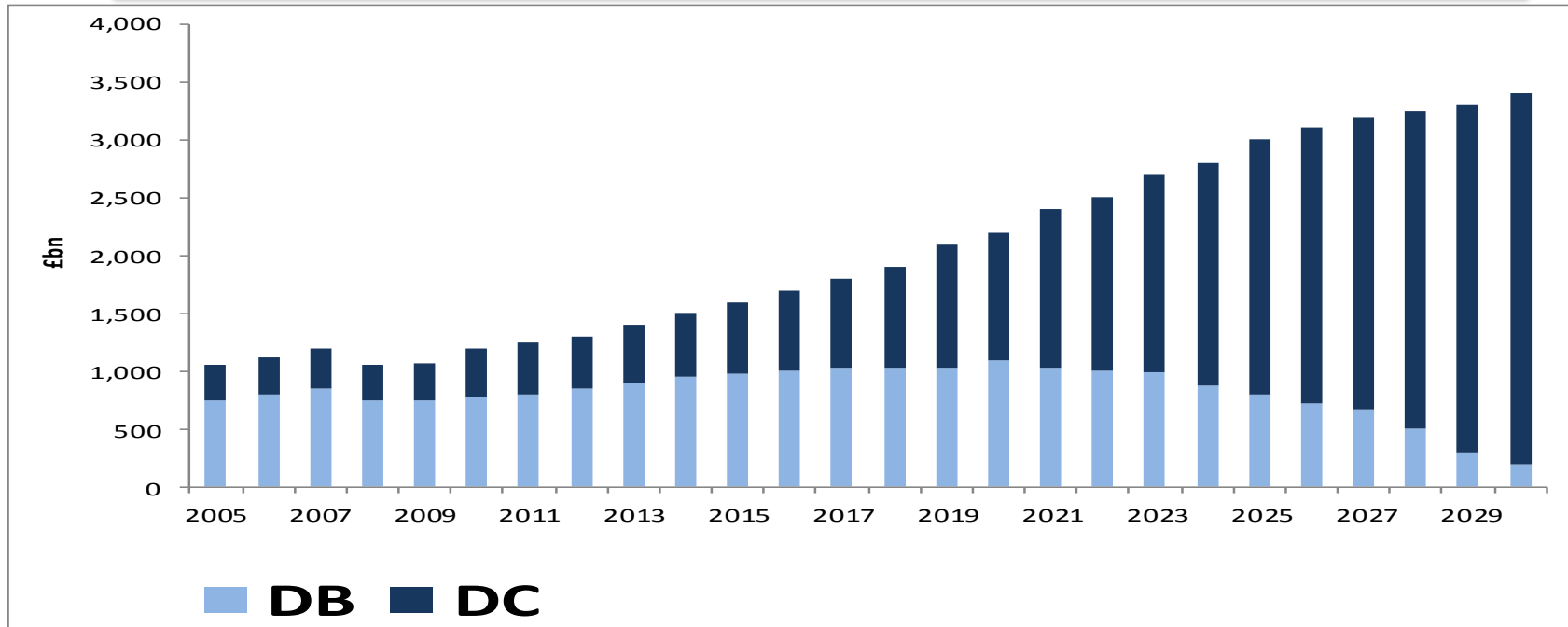


*Other includes Drawdown, Cash, Equity Release (Lifetime Mortgages) and Alternative products.

**L&G Estimates.

MEETING CUSTOMER NEEDS IN RETIREMENT.

PROJECTED GROWTH IN DC



Success criteria for retirement product providers

- Effective customer engagement before, at and in retirement
- Route to good value advice
- Range of product solutions addressing customer needs
- Good at adapting to change



Questions



Comments

Expressions of individual views by members of the Institute and Faculty of Actuaries and its staff are encouraged.

The views expressed in this presentation are those of the presenter.