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Decumulation in Europe

A 16 Country Perspective

Actuarial Association of Europe Taskforce on
Decumulation

Chair: Duncan Robertson

16 November 2015



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AAE Decumulation Taskforce Survey of Member States Product Gaps

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AAE Decumulation Taskforce

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Terms of Reference

- Taskforce created by AAE early 2014 reporting to Pensions Committee to:
 - Generate output that will influence and educate EU institutions
 - Position paper assessing various decumulation solutions
 - Complete the task by early 2015

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Taskforce membership

Name	Country	Employer
Louise Evans	UK	The Pensions Regulator
Ken Forman (Former Chair)	UK	AAE IFR committee
Esko Kivisaari	Finland	Chair, AAE Insurance C'tee
Ágnes Matits	Hungary	Pensions C'tee
Waheeda Narker	UK	Towers Watson
Duncan Robertson (Chair)	Ireland	Aegon

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Decumulation

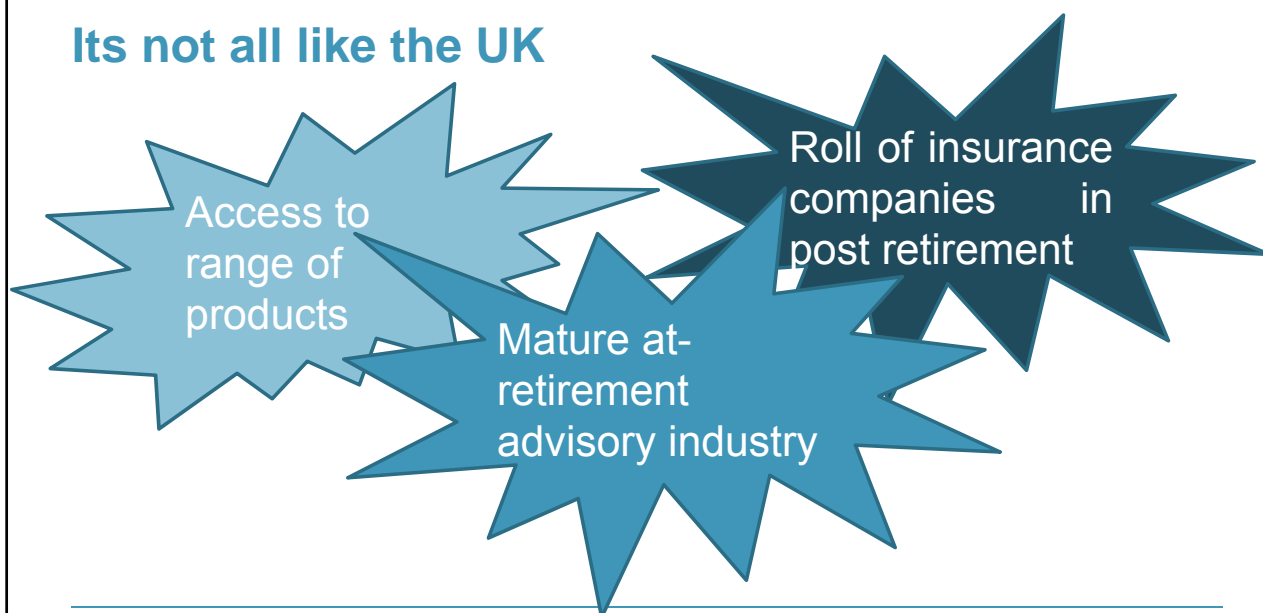
“The method by which an individual accesses their pensions entitlement/retirement benefits to meet their financial needs in retirement.”

- This is distinct from “accumulation”, which is the stage where the individual builds up his/her entitlement
- There can be overlap between accumulation and decumulation solutions, e.g. a ‘life-styling’ investment strategy

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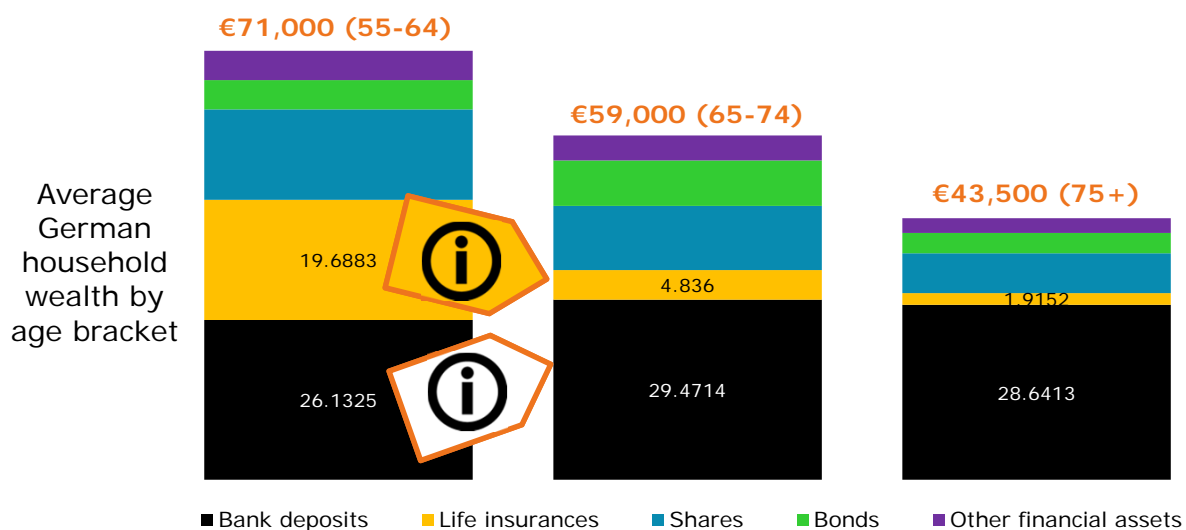
Its not all like the UK



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Germany – make up of assets



Source: Deutsche Bundesbank, as of June 2013

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Survey of Member States



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Target Audience

- Main target for the report was DG for Employment, Social Affairs and Inclusion
- DG focussed on best practice across member states, fair treatment for all
- DG wanted to better understand the decumulation landscape across Europe
- DG main request was a survey of EU countries bringing out policy issues



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Survey of AAE Members

- Aims to provide information about the decumulation landscape in each member organisation's jurisdiction:
 - What currently exists?
 - Is it suitable?
 - If not, what would the ideal system be?

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Responding Member Organisations

- 16 member organisations responded

Member Organisations (by territory)

Catalunya	Lithuania
Croatia	Norway
Estonia	Portugal
France	Serbia
Germany	Spain
Hungary	Sweden
Ireland	Switzerland
Italy	UK



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Structure of Survey

- The survey was divided into three main sections:

Information on current arrangements

- Information on the form of current decumulation arrangements

Suitability of current arrangements

- Qualitative questions on the appropriateness and effectiveness of current decumulation arrangements

Ideal decumulation system

- Seeking views on what the ideal decumulation system might look like

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Member State Differences

- Different stages of maturity in different EU markets driven by:-
 - Extent of State provision
 - Significance of employer sponsored pension arrangements
 - Importance of defined benefit pensions
 - Maturity of voluntary pension arrangements
 - Tax rules
 - Depth of long dated highly secure debt instruments
 - Availability of expert, affordable advice for consumers
 - Different cultural preferences of consumers

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Member state comparisons

- Member states that have traditionally depended heavily on state pensions have largest gaps between current and ideal decumulation system
- Member states that have greater reliance on occupational and private pensions tend to have more developed markets
- All states have some gaps between current and ideal practice



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Key Themes of Survey: Gaps

- What individual needs are not met under the current arrangements?
 - If insufficient funds accumulated then there can be no miracle decumulation solution
 - There is a lack of product solutions that offer required flexibility but also provide consumers with protection against unforeseen events
 - Lack of information on decumulation issues and risks that consumers need to consider
 - Consumers have insufficient access to advice on which solutions meet best meet their own individual circumstances when making decumulation decisions
 - Lack of product that address extreme or special life circumstances

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Key Findings of Survey: Ideal Decumulation System

Choice	<ul style="list-style-type: none"> • Consumers should not be forced into one solution
Different solutions for different needs	<ul style="list-style-type: none"> • Individual circumstances should drive different solutions • Different needs occur at different life-stages
Good regulation	<ul style="list-style-type: none"> • Solutions need to be regulated • Clarity required between roles of state and individuals' needs
Access to good advice	<ul style="list-style-type: none"> • Good quality advice is required to help individuals plan their retirement
Tax incentives	<ul style="list-style-type: none"> • Tax incentives are required to encourage and reward individuals for saving for their retirement

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Response from DG Employment

- Survey was well received
- Two follow up requests



Gain better understanding of decumulation products and product gaps

Does cross border insurance offer opportunities to fill any gaps?

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Decumulation Product Gaps

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Product Gaps: Types of Product

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Decumulation Products

Decumulation Products

Financial arrangements that are promised to or purchased by an individual for the purposes of decumulation

- Purchased prior to, at, or following an individual ceasing their working lifetime
- Accessed after they have stopped working
 - May be subject to eligibility criteria
- Cash lump sums and/or income

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Three Broad Types of Products

Annuity

- Fixed term or the rest of the person's life
- Level or increasing
- Single or spouses benefits

Drawdown

- Aka phased withdrawals
- Pension pot invested in bank deposit or investment funds
- Withdrawals taken from the bank deposit/funds

Guaranteed drawdown

- Pension pot invested in funds and withdrawals taken from fund
- Product provider guarantees capital amounts and/or income for life if fund is exhausted

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Product Gaps



Needs and wishes
of consumers

MIND THE GAP



Solutions that
products deliver to
consumers

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Product Gaps - Customers

Different individual's may place greater or lesser emphasis on the following needs



Guaranteed income



Bequests



Flexibility



Accessibility



Tax efficiency



Value for money

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Customer – Gaps

Needs	Annuity	Drawdown	Guaranteed Drawdown
Guaranteed Income	✓	✗	✓
Bequests	✗ - generally	✓	✓
Flexibility	✗	✓	✓
Accessibility	✗	✓	✓
Tax Efficiency	✓	✗/✓	✗/✓
Perceived value for money	✗	✓	✗

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Customer Needs – Annuity

Pros	Cons
+ Guaranteed income – level, increasing, spouses	– One off decision, can't change mind
+ Can be underwritten	– Inflexible - little ability to change level of income, take ad-hoc withdrawals
+ Annuity can be “cheap” when purchased	– Limited death benefit options
+ Females benefit from unisex rates	– Annuity could be “expensive” when purchased
+ Needs no management post sale	– Males get poorer value from unisex rates

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Customer Needs – Drawdown

Pros	Cons
<ul style="list-style-type: none"> + Invested money gives potential for growth + Can change income level + Death benefit options + Bank deposit drawdown provides capital “guarantee” + Able to phase decumulation + Able to purchase annuity when time is “right” 	<ul style="list-style-type: none"> – Income not guaranteed for life – Low growth in bank deposits increases risk that fund will run out – Poor fund performance increases risk of fund running out – Sequence of return risk – Risk of living “below one’s means” – If used to delay annuity purchase there is no guarantee rates will improve – Too much choice can confuse customer – Needs ongoing management

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The chance of running out of money

Persönliche Übersicht - einfach und nachvollziehbar

Bei einer Anlage in eine Aegon Secure *DepotRente*:

Ihr jährliches garantiertes Mindesteinkommen ist: 5.057 €	Ihr jährliches garantiertes Mindesteinkommen könnte steigen, wenn sich die Märkte gut entwickeln.	Und ist für den Rest Ihres Lebens garantiert.
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Bei einer Anlage in ein Sparkonto:

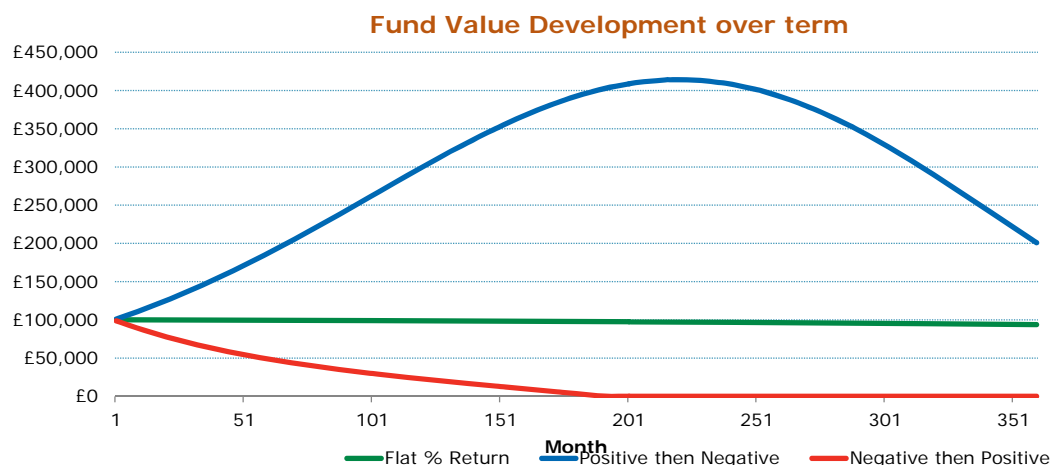
Bei einer jährlichen Entnahme von: 5.057 €	Die Hälfte Ihrer Anlage ist aufgebraucht im Alter von: 77	Ihre gesamte Anlage ist aufgebraucht im Alter von: 87	Die Wahrscheinlichkeit, 87 Jahre alt zu werden, ist größer als: 1 zu 2
Die Wahrscheinlichkeit, 95 Jahre alt zu werden, ist: 23%	Bei einer Finanzplanung bis zum Alter von 95 fehlt Ihnen in diesem Szenario dieses Einkommen für:		8 Jahre

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Sequence of returns risk

Scenarios taking 4% of investment + 1% (of fund value) in charges



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Customer Needs – Guaranteed Drawdown

Pros	Cons
<ul style="list-style-type: none"> + Guaranteed income + Ability to alter income level + Death benefit options + Fund remains invested so potential for it to grow + Ability to move to decumulation stage gradually + Ability to buy annuity when time is “right” + Females benefit from unisex rates where Gender Directive is applicable 	<ul style="list-style-type: none"> – Cost of the guarantee – Benefit of the guarantee reduces in a rising market unless product contains a guarantee that increases in rising markets – Males get poorer value from unisex rates where the Gender Directive is applicable – Can be complicated products to understand

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Product Gaps - Providers

Different products place different challenges on providers



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Provider Needs – Annuity

Pros	Cons
<ul style="list-style-type: none"> + Generally a good supply of annuity products from insurance companies + Offered for a long time and are relatively well understood + Where annuitisation is compulsory there is a captive market + Investment risk can be reduced through asset matching and profit participation 	<ul style="list-style-type: none"> – Both investment and longevity risks – ALM of residual investment risk is complex – Longevity risk is difficult to manage – limited reinsurance – Generally only offered by insurance companies

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Provider Needs – Drawdown

Pros	Cons
<ul style="list-style-type: none"> + Providers can retain any accumulated funds under management + Lifetime product to customer + Providers do not take on longevity risk + Investment risk is limited to impact on fees + Many types of financial institutions have the expertise to manage drawdown products 	<ul style="list-style-type: none"> – Reducing fund means reducing profit income streams – Reputational risks where customers run out of money – Challenges interacting with aging customer with reducing cognitive reasoning functions – Persistency risk from customers moving business between providers

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Provider Needs – Guaranteed Drawdown

Pros	Cons
<ul style="list-style-type: none"> + Less reputational risk of customers running out of money + Less reputational risk from customers wanting access to their money + Customers more likely to remain with provider as guarantee is lost if funds moved + Less need to seek decisions from aging customer 	<ul style="list-style-type: none"> – Providers take on longevity and investment risk – Managing longevity and investment risks is very complex – Requires specialist expertise and day-to-day hedging programmes – Limited number of providers with necessary expertise

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Product Gaps: Cross Border Insurance

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EU Cross Border Insurance

- Consolidated Life Directive (2002/83/EC) entitles insurance companies authorised in one EU Member State to write insurance business in other Member States
 - This is retained in the Solvency II legislation
- Traditionally dominated by two EU member states
 - Ireland and Luxembourg
 - However, a number of other EU member states are increasing their presence, e.g. Malta, Cyprus

€38bn

of cross border
premium income
written in Ireland
and Luxembourg in
2013

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Cross Border a solution to Product Gaps?

- Theory:

- Product solutions and product gaps vary from country to country
- Solutions may exist in one country that could usefully fill a product gap that exists in another country
- Cross Border insurance allows products designed in one EU member state to be available in another member state

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Cross-Border Solutions that drove innovation

UK Fund Supermarkets / Platforms

- Offered UK customers access to a very wide range of fund options from early 1990's
- UK companies responded to customer need initially by offering similar solutions and then enhancing the customer experience.

Italian Unit Linked Business

- Successfully delivering new innovative unit-linked solutions to Italy since late 1990's
- Utilised skills, expertise and operating model infrastructure developed for other markets to deliver solutions to the Italian market.

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Cross-Border Solutions that drove innovation

Scandinavian Annuities

- Developed innovative annuity solutions for Scandinavian customers until mid 2000's
- Annuity products now launching in the UK are similar to those designed 20 years earlier for the Scandinavian market

Guaranteed Unit Linked Products

- In the mid 2000's US companies created Irish companies to sell guarantee products into other EU member states
- These companies are now offering Guaranteed Drawdown solutions into the UK

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Product Gaps Conclusion for DG

- Three main decumulation product types

Annuity

Drawdown

Guaranteed
Drawdown

- Each product type offers pros and cons both to consumers and the providers of these products

Product Gaps can be filled by:

New products offered by
existing providers in that
market

or

Existing products from other
markets, offered on a cross-
border basis, to consumers

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Summary

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Summary

- Survey of 16 member states
 - Identified common gaps in current decumulation systems
 - Identified main requirements of an ideal decumulation system
 - Identified common themes behind level of maturity of decumulation market
- Products Gaps
 - Overview of different product types
 - Potential for cross-border insurance to support filling any product gaps
- DG for Employment, Social Affairs and Inclusion better informed on issues



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Questions

Comments

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