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The Over 50s Rip Off!

A reprise looking at the market for annuities post 6 April 2015

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How have the insurance industry and its customers changed following the implementation of Pensions Freedoms?

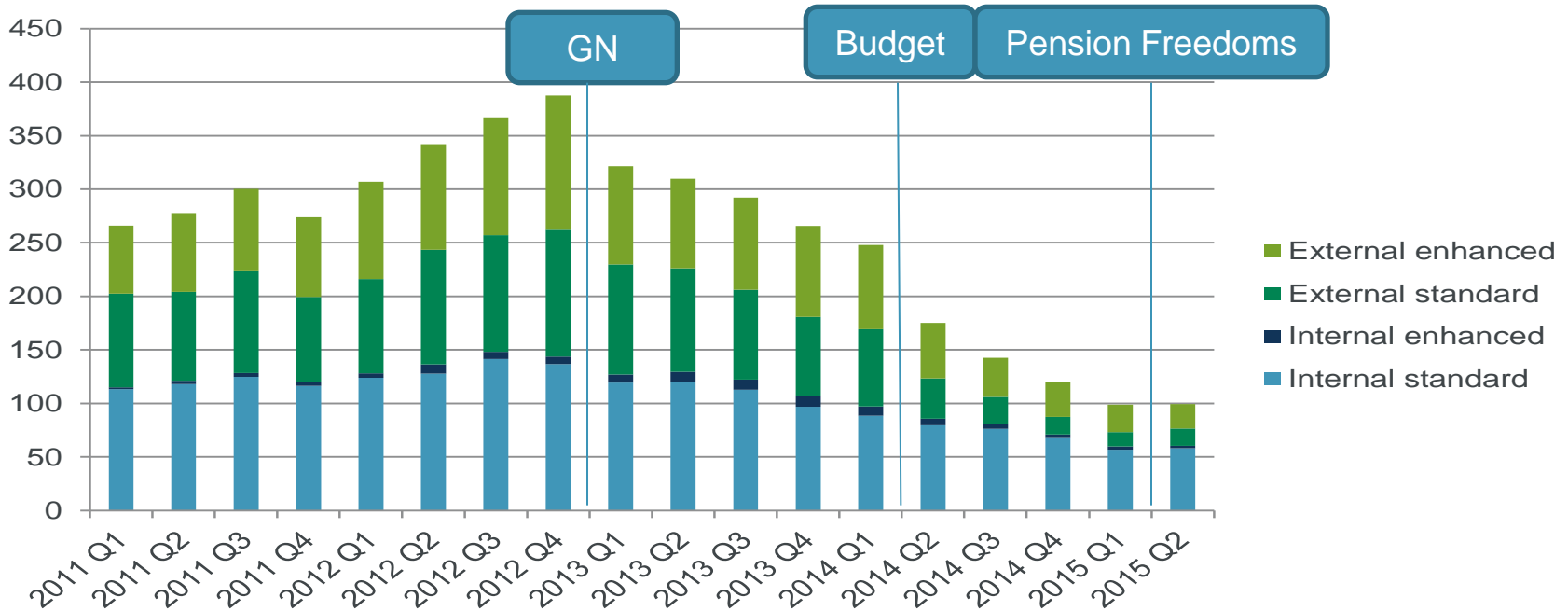
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ponsorship
Thought leadership
Progress
Community
Sessional Meetings
Education
Working parties
Volunteering
Research
Shaping the future
Networking
Professional support
Enterprise and risk
Learned society
Opportunity
International profile
Journals
Support

Outline of talk

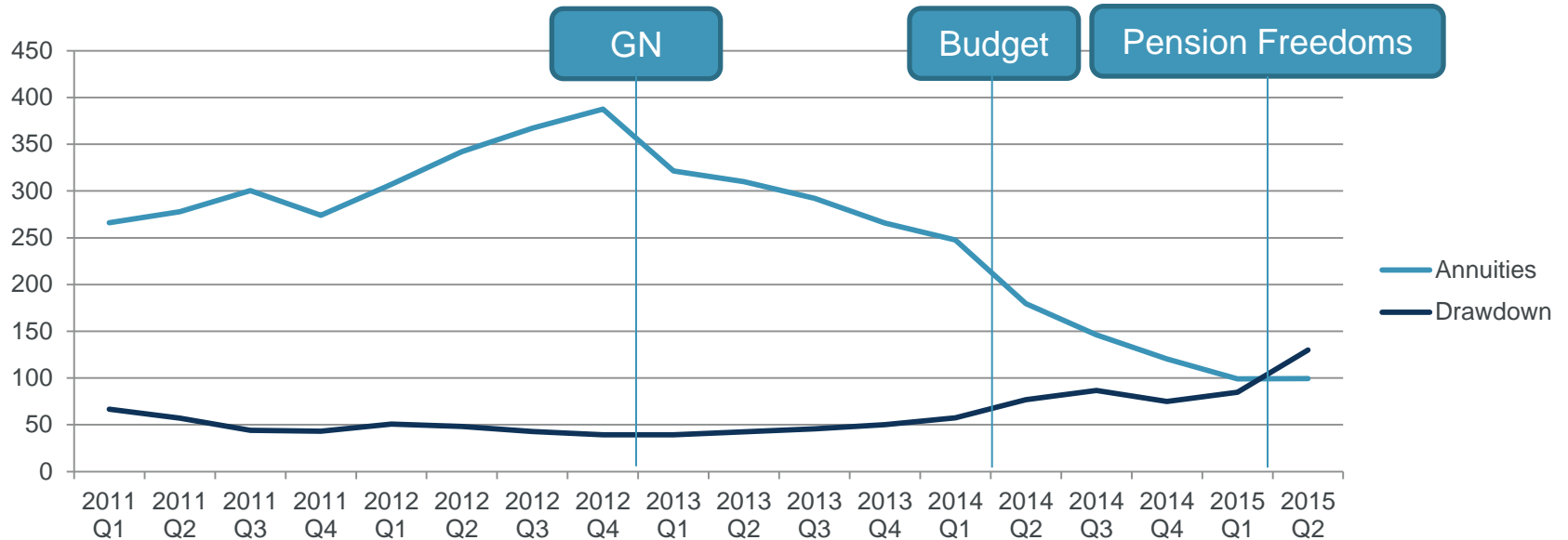
- Facts
- Inferences
- Predictions
- Influences on the 'End State'
- Key Messages

UK Annuity market experience (ABI)



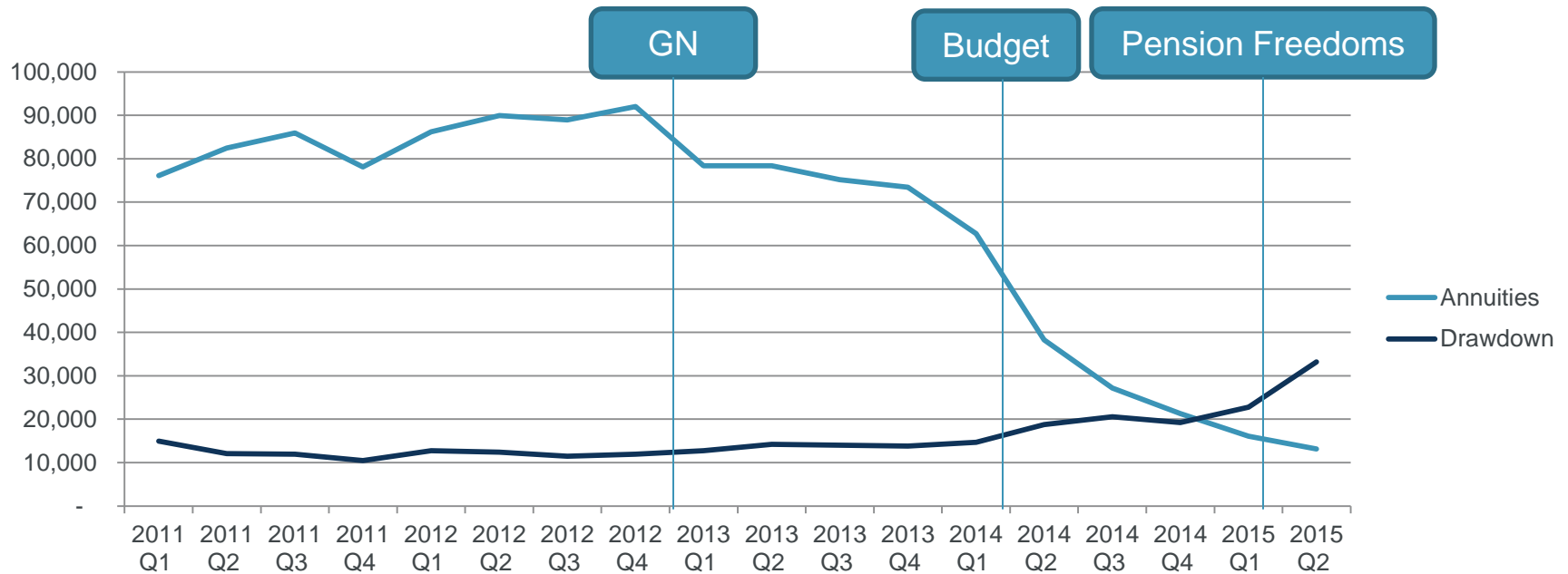
- Annuity sales were in decline before the 2013 budget but the data shows a marked decline following the announcement of pension freedoms with the impact falling most heavily on open market sales
- Sales stabilised in Q2 2015 following a long period of decline however this may have been influenced by customers deferring decisions leading up to the implementation of pension freedoms

UK Drawdown market experience (ABI)



- The significant decline in Annuity sales has been only very partially offset by the growth in Drawdown sales
- Drawdown sales exceeded Annuity sales for the first time in Q2 2015
- A significant proportion (45%) of drawdown policies are taken from the customer's existing pension provider

UK Drawdown market experience (FCA)

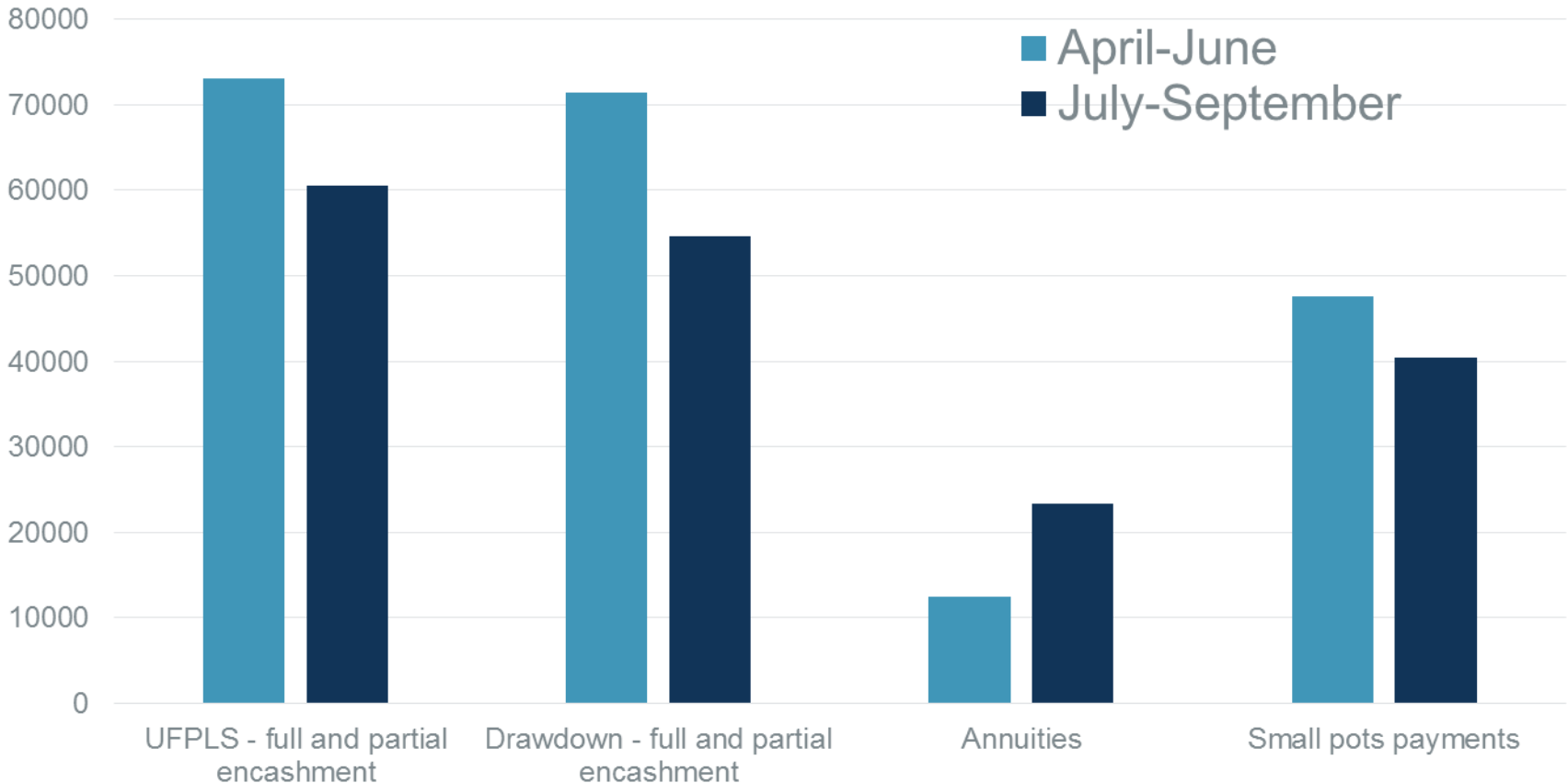


Consumer choices

FCA (January 2016)

- 380,000 people accessed pension pots in the first 6 months since the reforms, roughly double the number in the same period in 2013
- Over the same 6 month period there were c35,000 annuity sales in 2015 compared to 180,000 in 2013
- Of the remaining 345,000, around 2/3rds opted for cash withdrawal and 125,000 had accessed some form of income drawdown product. This compares to around 20,000 taking cash or drawdown in 2013.

Consumer Choices – April to September



Other data sources

Pension Wise

- 43,000 Pension Wise appointments between April 15 and February 16
- Citizen's Advice completed 3,215 face-to-face appointments in January compared to the peak month, October, of 5,343
- Statistics suggest that fewer than **one in ten people** accessing their pots had a Pension Wise session
- The FCA told the Work and Pensions Committee in July that Citizen's Advice was running at 10-15% of its capacity to provide face-to-face appointments.
- The number of appointments has continued to fall and the cost of each appointment has risen steadily. Adviser numbers are now falling

Other data sources

ABI (October 2015)

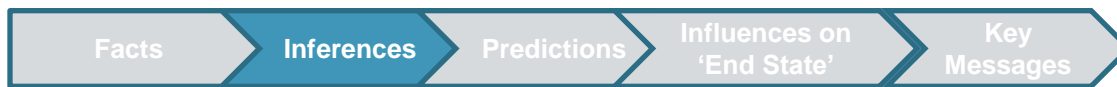
- In 95% of cases where savers accessed a cash lump sum, they withdrew the entire fund

Standard Life (October 2015)

- In Q3, c90% of customers with pots less than £30,000 have just taken cash

FCA (January 2016)

- Shopping around rates remain low, with just 42 per cent of drawdown customers and 36 per cent of annuity purchasers switching providers.



Inferences

The Obvious

- Demand for annuities at retirement has decreased significantly and will remain significantly below pre-Freedom levels
- This is particularly pronounced for low fund values due to the increase in triviality limits
- Pensioners are attracted by the greater freedom and control that they achieve through non-annuity solutions such as drawdown or taking cash

The Likely

- Many customers are making decisions without any advice
- More pensioners will experience periods of sub-optimal pension income during their retirement either as a consequence of drawing down too little income (for the risk averse) or too much too soon (for the risk takers)



Inferences

The Likely (cont'd)

- The value chain for at-retirement advice and solutions has shifted again as illustrated below:

| | 1990's | 2000 - 2012 | 2013 – Q1 2015 | Current |
|---------------------------|--|--|---|--|
| Market conditions | <ul style="list-style-type: none"> Pre-RDR Low take-up of OMO Standard annuities dominate | <ul style="list-style-type: none"> Pre-RDR Increasing awareness of OMO Advent of enhanced annuities Just Retirement & Partnership market entry | <ul style="list-style-type: none"> Post-RDR OMO overtakes internal annuity sales Enhanced annuities account for c1/3rd of sales | <ul style="list-style-type: none"> Post-RDR Post Pension Freedoms SII looming |
| Annuity Providers | Good margins | Margins remain good although some erosion | Further erosion but still an attractive market | Very challenging market conditions |
| Financial advisers | Good margins where advice taken | Improved margins and growing demand for advice | Polarisation of advice market between fee based wealth managers catering for large funds and non-advised annuity specialists catering for small/medium funds | Good margins for advisers with Wealth Management, Platform and consolidation focus. Annuity specialists switching focus to Equity Release. Some momentum behind robo-advice to cater for the masses. |

Predictions

- The current state is likely to be short-lived. Few market commentators believe that the market as it stands is effective and is adequately serving the best interests of customers.
- The Work and Pensions Committee undertook an inquiry to take an early look at the impact of pension freedoms. The report from that inquiry, issued in October, included the following conclusion:

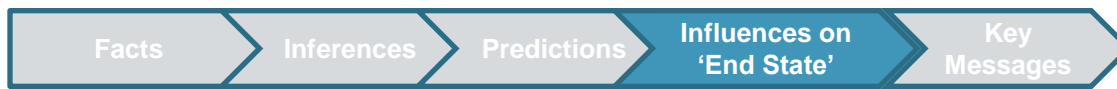
'A watching brief on pension freedom is imperative and we intend to return to this issue over the course of the Parliament.

Whether improvements in the quality and take-up of guidance and advice can be achieved will be central to the success of the policy. It is right that people should be able to choose what to do with their retirement savings. However, **freedom to choose is not enough; people must have freedom to make informed choices.'**



Predictions

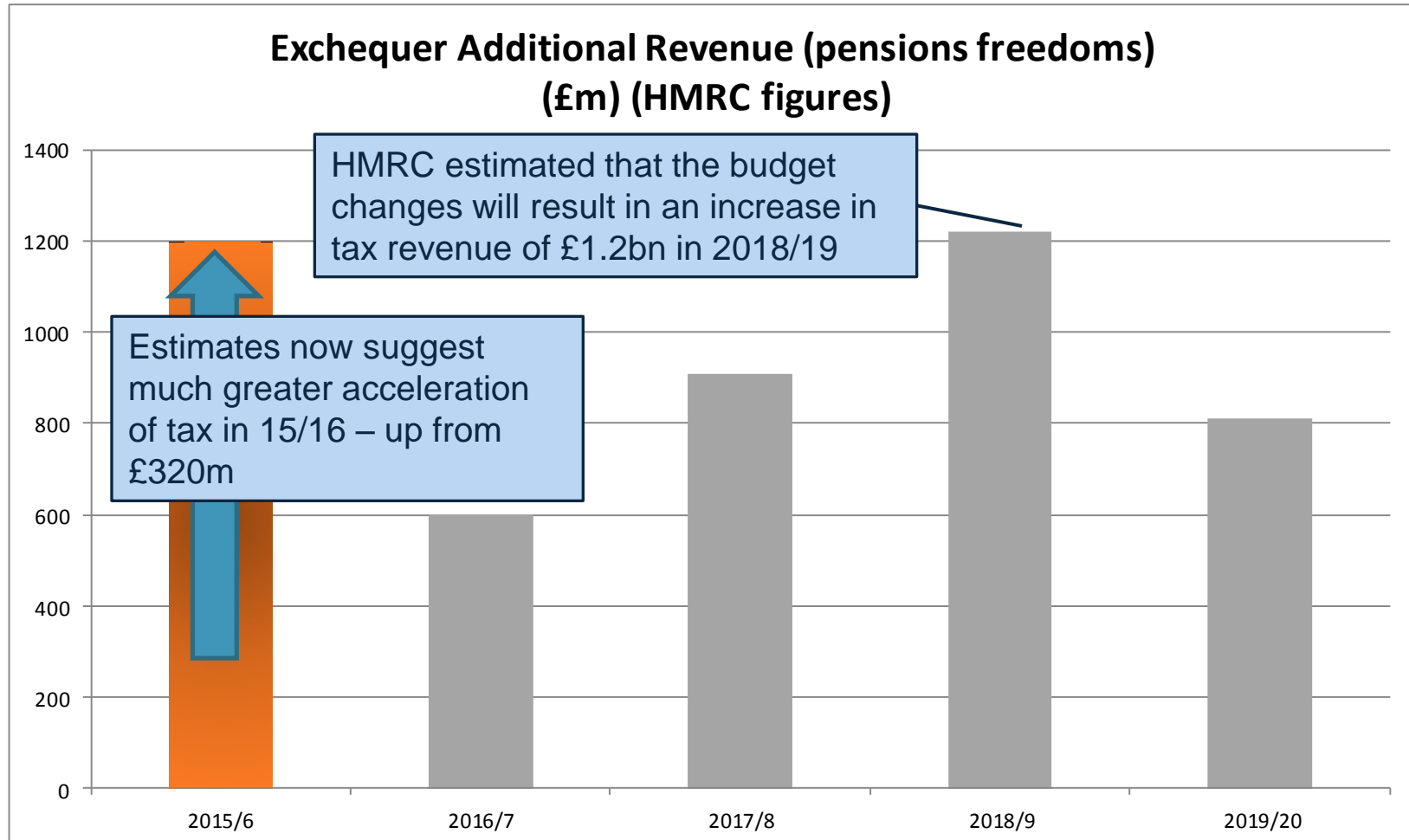
- There are a number of factors that are likely to evolve and the pace and extent of evolution of these factors will determine how the market develops. These factors include the following:
 - The media response
 - Default options
 - Stock market volatility/performance of target return type funds
 - **Provider innovation**
 - **Interaction of Government and Private pension provision**
 - **Customer engagement (including advice)**
 - **“Left field” – the unknowns**



Developments in the retirement market

- Blended approach
 - mix of drawdown and annuity products
 - Or even wider mix of potential products healthcare/disability/spouse/..
- Multi-asset income funds – high income and capital preservation
- Phased funds – decumulation followed by annuity
- With-profits pensions revamp
- “Pension bank account”
- Pension ISA

Tax and Pensions Freedoms



Retirement freedom around the globe

| | Australia | Chile | Ireland |
|--------------------|---|--|--|
| Freedoms available | Drawdown Annuity Lump sums | Drawdown Annuity Deferred annuity Combinations | Drawdown Annuity |
| Tax treatment | T-T-E No tax on exits | Essentially E-E-T Voluntary contributions could be E-E-T or T-E-E | Tax free lump sums Tax on drawdown encourage 5%pa withdrawals |
| Comments | Very few annuities taken State pension means tested but property doesn't count | Annuities have 60% take up rate Quote system operated by regulator | Annuities have 30% take up rate Minimum income limits apply |

Melbourne Mercer Global Pension Index

Sponsored by Victoria State Government, October 2015

Includes both government and private elements of each of 25 country's pension system.

For each country's pension system MMGP Index looks at 40 different indicators grouped into 3 areas:

- Adequacy (40%)
- Sustainability (35%); and
- Integrity (25%)

UK is in 9th position (score reduced from last year due to Pension Freedoms) behind Chile and Australia, but just ahead of Ireland (11th place)

Denmark in pole position.

Strengthening the incentive to save: a consultation on pension tax relief

- Currently incentivisation is in the form of tax relief of pension contributions at marginal rates
- Tax is levied during the lifetime of a pension plan as follows in simple terms:
 - Contributions attract tax relief (i.e. exempt from tax)
 - Interest and gains on the investments are exempt from tax during accumulation
 - Tax free lump sum is available; and
 - Pension income is taxed at marginal rates once fund is accessed
- Referred to as an “E-E-T” system

Strengthening the incentive to save: a consultation on pension tax relief

- Radical proposals to change from E-E-T to T-E-E, or perhaps more again in simple terms:
 - Up to a maximum i
- Flat rate tax relief contributions attract the same level of independent of marginal tax

Postponed?
- Pension
 - M than the ISA
- Lifetime ISA introduced in Budget 2016



Customer engagement – challenges

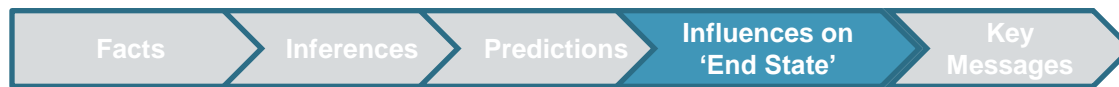
- Advice and guidance
 - 48,000 guidance appointments (end-Feb)
 - 2.1m PAS website visits (some of them mine!)
- Policyholder communications (e.g. wake up letters)
 - Must not obscure Guidance
 - Providers may be too directive? FSCP comments
- “Pensions Passport”?
 - Simplify and standardise information from providers
 - Policyholders use the passport to obtain guidance/robo-advice/advice
- “Pensions Dashboard”?
 - To pull together all information from different providers

Customer behaviour – cash-hoarding?

- Savers withdrew £4.7bn from pension pots in the first six months of the new freedoms, according to the Association of British Insurers.
- £2.5bn has been paid out in cash lump sums, with an average payment of around £15,000 (ABI, same period).
- Figures from FCA show c380,000 policyholders accessed their pensions in period April- Sept
 - Most taking cash – c35,000 annuities purchased (down from 180,000 in same period in 2013)
- Pensions and Lifetime Savings Association – recent survey suggests only 18% taking lump sum have spent it

Customer engagement – complaints

- The number of pension complaints has risen 20 per cent in the last six months, FCA data reveals.
- The latest complaints data from the regulator shows there was a total of 73,055 complaints about decumulation, life and pensions products between January and June 2015.
- FOS received 1,080 complaints concerning pensions freedoms to end-February
- Complaints include
 - Need for advice before cash paid out (e.g. on GARs)
 - Inability to cash-in an annuity (see later!)



Customer engagement – complaints

| Firm | Number of new complaints (H1 2015) |
|--|---------------------------------------|
| Prudential Assurance | 8,827 |
| Friends Life | 7,013 |
| Royal London Mutual Insurance Society | 5,688 |
| Aviva Life Services UK | 4,342 |
| Scottish Widows | 4,110 |
| Zurich Assurance | 4,004 |
| Scottish Equitable | 3,826 |
| Phoenix Life | 3,554 |
| Legal & General Assurance Society | 2,609 |
| Abbey Life Assurance | 2,543 |

Customer engagement (including advice)

Secondary Annuity Market

- Government has now unveiled details of the creation of a Secondary Annuity Market
- Follows consultation earlier in 2015 - another element of Pensions Freedoms
- May be a significant “backlog” of sellers initially
 - Purchased annuities in recent years with small pots
 - Don't need the income stream as enough from other sources
 - Want to gain access to the wider freedoms, to re-invest in drawdown etc
- But will this last for more than a few years?

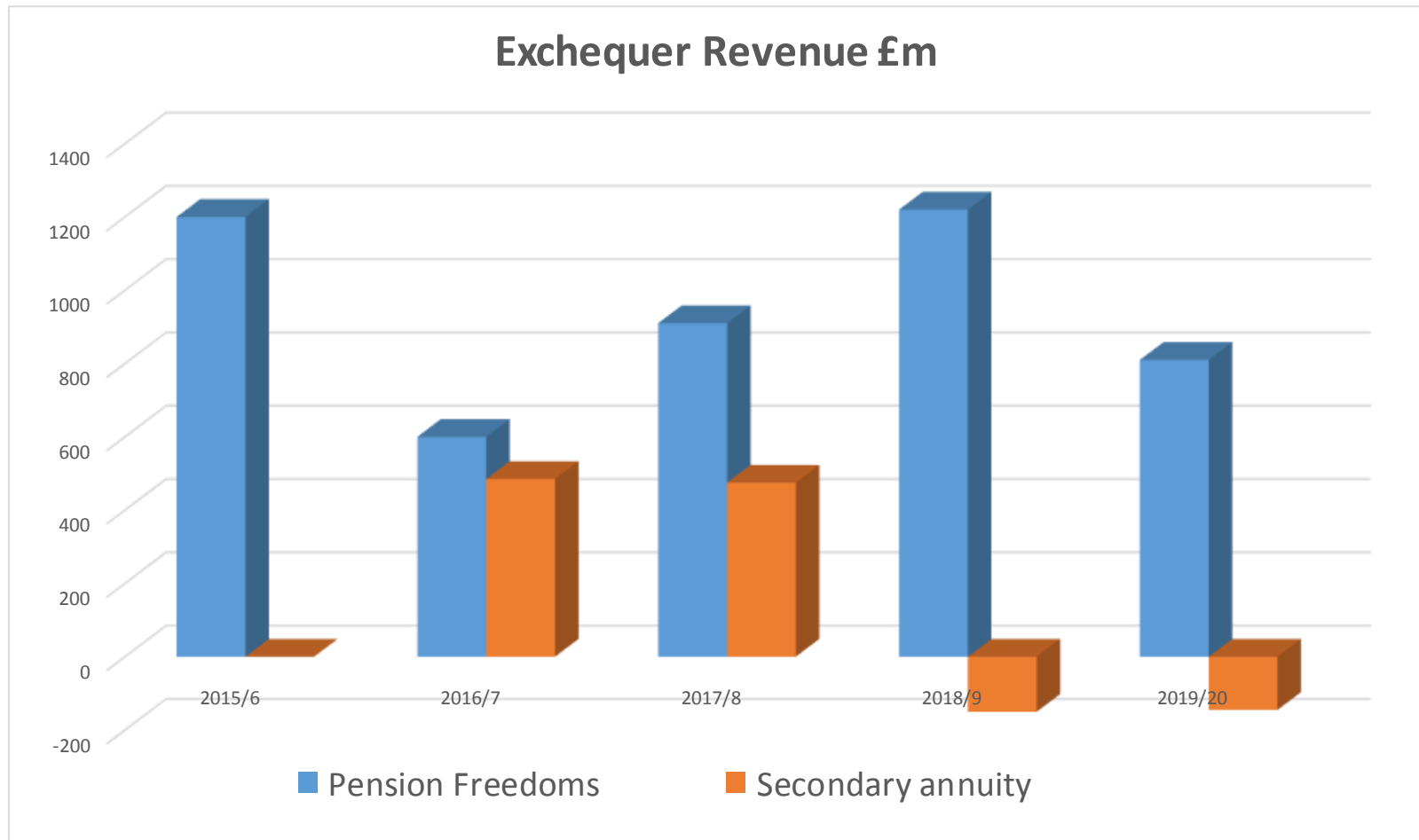
Secondary Annuity Market

- Infrastructure
 - Much debate has focused on how the buyers and sellers will come to market
 - Intermediated process
 - Original provider allowed to buy back
 - Small annuity buy back direct – threshold to be confirmed
- Buyers (to be authorised by FCA) are likely to include:
 - Main annuity players
 - Pensions schemes, new entrants?
- Tertiary market may emerge

Secondary Annuity Market

- Policyholder protection
 - Advice above a threshold level
 - Guidance via Pension Wise
- Other areas under consideration
 - Tax basis – consultation on details in 2016
 - FCA rules – consultation in 2016
 - FCA portal?
 - Dependants, beneficiaries, “any spouse”?

HMRC's view of secondary annuity market



Key Messages

Still more change to come

- Industry still catching up with changes and may be greater innovations to come
- Policyholders unsure where to go for advice and may not be getting optimal solutions
- Government and media concerns about current state of play – too much freedom?
- Secondary annuity market may add a further dimension
- Research shows interaction of Government and Private pension provision has a major influence on behaviour
- Pension tax relief is still a very hot topic

... despite all this there is still a place for the humble annuity and the insurance concept



Questions



Comments

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