

THE 75 DEBATE

The Treasury has issued a consultation paper replacing the alternatively secured pension regime and the 75 rule with flexible and capped drawdown and a requirement for clients to have a minimum income. The industry is now considering these changes and their implications for advisers, clients and providers.

With the consultation closing in September, advisers haven't long to debate the changes and perhaps suggest changes and the Retirement Partnership is aiming to help. As the first part of that process, the Retirement Partnership asked four industry experts for their initial thoughts and concerns.

Interviews by John Lappin

Barry O'Dwyer Deputy Chief Executive Prudential UK and Europe.

"With this consultation document, it is still clear that an annuity remains the most sensible means for most people to have an income in retirement. This paper is about giving more flexibility to a small group of people who can afford to wait until they are 75 to take their retirement income. It is still a broadly positive move, in that it gets rid of a reason that some people gave occasionally for not saving while bringing welcome flexibility for the top end of the market."

"It also makes sure that we are not going to have a silly situation where people were pushed away from the best product for them. For the vast majority that remains buying an annuity for retirement." "One thing we would like to see adopted, in particular, is the removal of restrictions on value protection annuities. This is something that we have championed for many years. One of the misconceptions about annuities is they are a rip off because "the insurance company keeps my money if I die." Value protection didn't really work with the age 75 restriction so it gives the chance to really develop a really good annuity product that appeals to more customers.

"There are some issues that advisers should start thinking about for instance on capped drawdown. If you don't go fully flexible or take a big lump sum from your pension, and you go down the capped drawdown route, there is a heavy hint in the document that the GAD max is going to go from 120 per cent to something lower. In some respects that will make drawdown less attractive for some segments of the retired population. That is something that advisers will be getting their heads round now.

"The tax rules are one area where we would like to see some movement too. The tax and death benefits after seventy five of 55 per cent are pretty hefty. It is based on the assumption that everyone who takes advantage of the full flexibility will have had higher rate tax relief on the way in. But that is a bit of an assumption. Fifty five per cent is obviously unfair if you have had 20 per cent relief on the way in.

"I think the Government's position is that it wants something simple as possible and a single rate of tax is simpler than working out whether a customer had received lower or higher rates of relief in the build up. As always in these things, it is going to come down to the detail, and one very significant detail is the minimum income requirement. The Government has not set this out and that is obviously going to affect the number of people who are going to be able to afford the full flexibility. That is a crucial issue to be determined over the course of the consultation."



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Aston Goodey, sales and marketing director at MGM Advantage

"This is a good move. It will help with the perception that exists where people think: "If I come to retirement, and I give my money to my insurance company and I die, they keep it." We know that is not the reality, but that is the perception. What people will now think is: "Great, I am not compelled to do something." It will also help at the accumulation stage, because people will think they can eventually do more with the money they are saving.

"It does come with some risks. There needs to be a health warning. With average pension pots around £25,000 need to maximise their income and most people need to do it for life. For the vast majority of people taking an annuity will be the right thing to do and realistically it is still the only option for many consumers.

"It is more likely to affect the high net worth end of the market rather than the middle or the lower end. In terms of the health warning, the problem is that what is not spoken about much and is not visible to some consumers and even some IFA's, is the mortality cross subsidy. The benefit of an annuity is you are part of a pool - those who die early subsidise those who live longer, and at age 77 it can represent an extra two per cent return on your fund.

"If you are not part of annuity pool, there is a cost to your fund growth. These figures are significant. But people don't see that, they think "Great I can go into this drawdown, because of the new rules. Great I can stay in drawdown and get these death benefits."

"They may need to take a step back. First they should ask do they not need an income. If they don't, you might ask why accumulate all that wealth in a pension in the first place, because it was not designed to provide a lump sum death benefit, but to provide an income in retirement.

"It is only the very, very rich that can afford not to take an income. Let's assume you need an income eventually, even if you defer it, there will be very few who wait till after 75. Some people may still be working, but realistically most people won't be by 75. If you want to maximise income, it is probably worth taking an annuity.

"However the change in perception will be great news. On products, there are opportunities. I think having a drawdown contract with a minimum amount of income required will lead to a particular product design.

"Impaired life will grow because the longer people leave it to take an annuity the greater chance they will be impaired. People will stay in drawdown longer. It is great ASPs are going and will help to simplify things.

"You will see cocktailing, i.e. a £100k fund may have an element of secured income in a conventional/impaired annuity and the balanced in something that is invested i.e. drawdown or asset backed annuity.

"From an adviser's perspective, it has created a massive focus on the area at a time when people reaching 65, is about to peak. I think this is tremendous news for the IFA population as consumers will need their help now, more than ever.

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Steve Lowe Living Time marketing director

"I am positive about the change overall. It delivers increased flexibility for a lot of people. But what I am most positive about is that the change will create a lot of noise and discussion about retirement options generally and specifically that there is no longer a need to annuitise for those that want to maintain control of their pension fund. It should lead people at the age of 65 to consider if annuitising at that early stage in their retirement is the right thing to do.

"As a result, it will help more than the roughly one per cent of people who currently defer their annuitisation until age 75. Being able to extend death benefits beyond 75 is an excellent extension to the current rules. What I suspect will happen on the manufacturing side is that we will see product innovation, leading to the creation of some creative new customer solutions.

"On the minimum income, the kinds of numbers being debated are in the £200,000 to £300,000 range. The big question is whether we should be forcing people to secure a lifetime income from just their pension assets. I know the fear is people will fall back on the state and yet I question whether that should always mean they must rely on something like an index linked annuity. There is certainly a case for alternatives in the consultation. People should still be allowed to re-set their options and escape the 'lifetime sentence' that shackles so many people today.

"On the capped annuity, we see it like you have today with an unsecured pension product where you are pretty much constrained in what you can take. Part of the key to unlocking the best outcome from the consultation is having a rigorous discussion about where the Government sets those limits, rather than the mechanics. The mechanics are pretty straight forward. Of course, the new proposal is far better than the alternatively secured pension regime but we need to make sure the cap isn't too prohibitive."

"But the area we see as most important is challenging the need to have an income that is index linked for life. We would hope the Government looks at options other than an annuity or at least at having break points for customers to enable them to re-set their retirement benefits. From age 75 customers start experiencing an increase in the incidence of serious health conditions. If you secure a healthy life income at 75, then your body starts giving up, you are stuck in a poor deal. Today for customers sleepwalking into a lifetime annuity they are in danger of locking into a product class where rates are at a 30 year low. They don't have to do that, but most customers do not have the alternatives explained to them in a way they understand. We have to ensure we help them choose product solution where they understand they can get out and go back in with another option later in retirement as their circumstances and needs change.

"There has been a lot of excitement around the consultation but unless we get the OMO scrapped and replaced with what we refer to in the Pension Income Choice Association as a "Pensions Passport", then I think there is a danger it will have a much smaller impact than ministers are hoping. I urge them to get the law changed quickly to make this passport and shopping around mandatory. This will improve outcomes for customers and Advisers. If pension minister Steve Webb does the two things together then there is a chance to be a hero and unlock billions of pounds for the benefit of customers and the Treasury."

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Stewart Dick, head of sales Hornbuckle Mitchell

“The fact you have the coalition trying to find innovative solutions is admirable and very encouraging. But I would caveat that with a warning flag in that, while the capped and flexible proposals have a lot of merit, the Government has to be very careful that they don't make things overcomplicated. The vast majority of things we have seen since A-day have made things overcomplicated and we don't want to fall into the same trap again.

“I can see what they are trying to achieve with a minimum income, they don't want people to fall back on the state, but what we would like to find out is what that minimum is made up of, what can and cannot be included other than lifetime annuities.

“I also hope they have done the maths behind this on the tax take. The government has made a welcome commitment to review the anti-forestalling mess if they can achieve the same result in terms of tax - I hope they've done the sums on this as well so we aren't disappointed by any future U-turns.

“It removes a couple of barriers for us in the SIPP market. At the moment we still have people saying why should we invest when the tax rate is so penal? If these tax problems are removed we should see some interesting things in terms of product development.

“While we welcome the reforms as a great step there are still question marks. It comes back to keeping things simple in terms of allowing clients to understand the system and allowing companies to design things and advisers to advise on things that people want.

“I am hearing a lot of talk along the lines of ‘this will happen, this won't happen, this will be a requirement, this will not be a requirement’ but nothing is yet set in stone. So while we are excited, let's not get carried away. From an adviser's point of view, the basic requirements of retirement planning still apply. It may make things easier but it doesn't remove the need for compliant advice.”