

Understanding the risks at-retirement

✔ **Retirees now have more freedom and choice regarding their pension pot than ever before, but with that increased freedom comes increased risks. Jonathan Watts-Lay discusses these risks**

There is no doubt that freedom and choice in pensions is liked by many individuals but it has also increased the risks and complexity for all. Employees and members now face a whole host of issues such as falling for a scam, paying more tax than necessary or not understanding the risks around defined benefit pension transfers, and ultimately not optimising their retirement income.

With this in mind, let's take a look at some of the risks.

Tax

Over a quarter (27 per cent) of individuals over the age of 55 didn't realise that they have to pay tax on their pensions if they take the whole fund as a cash lump sum. This perhaps suggests why The Office for Budget Responsibility recently reported that the revenues raised from the pension freedoms in 2018 would be 50 per cent more than forecast and indicates that individuals are often paying tax when it could have been avoided with careful planning.

Scams

The FCA estimated that victims of pension fraud lost on average £91,000 each in 2017. Many are hoping that the new legislation making pension cold calling illegal will help the situation. However, individuals will still need to be alert as it's not going to stop all fraudsters, including those who are calling from overseas. Taking regulated advice

and getting the additional consumer protection it offers should not be underestimated.

Defaults at-retirement

Some in the pensions industry believe that default retirement pathways protect individuals from making poor decumulation choices. However, I don't believe that anyone should be defaulted at-retirement without receiving financial guidance and making a proactive decision first.

This view is supported by a recent poll by WEALTH at work, which found that 86 per cent of respondents believe that employees should not be defaulted into a decumulation pathway at-retirement without financial guidance.

Defaulting individuals into something without a positive choice being made raises questions over if it's within the pension providers or the member's best interest and the effects could be costly. After all, it discourages shopping around and risks destroying freedom and choice in pensions. Additionally, if those with more than one pension default based on individual pots rather than the collective value the likely outcome will be sub-optimal.

DB pension transfers

Defined benefit (DB) pension transfers have hit the headlines over recent times bringing member support under the spotlight.

Even though regulated advice must

be sought to transfer a DB pension if its value is £30,000 or above, there is no requirement to take ongoing advice and no guarantees that future income needs will be met.

Offering partial transfers can be an efficient way for schemes to manage liabilities and can also help members avoid the cliff edge of total transfer or no transfer. Only about 15 per cent of schemes provide this option now but our poll found that 85 per cent trustees and employers were in favour of all DB schemes offering it.

Guiding the way

Individuals really need to understand their options at-retirement, including the generic advantages and disadvantages of these, as well as considering associated risks such as tax inefficiency, longevity or losing money to scams.

Financial education and guidance at-retirement can help with this and will enable individuals to make informed choices, including being able to decide if they need further support such as regulated advice.

Although there are concerns over the take up of Pension Wise, nine in ten customers who received guidance were satisfied with the service. Our experience is that following financial education and guidance, employees emerge more confident, knowledgeable and more able to make informed decisions.

Employers and trustees are perfectly placed to facilitate access to a breadth of services including financial education, guidance and regulated advice, to help employees and members fully understand their options. However, there are still big gaps in the support available which is why we are calling for this provision to be made the norm.



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