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FINANCIAL EDUCATION

Understanding retirement income options – as easy as it seems?

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Last week I was talking to a colleague, a keen cyclist, about the impact of financial education and guidance on members' retirement outcomes.

He said there were many parallels between his take-up of cycling and becoming a competent cyclist, and what we do for employees during our financial education seminars.

Over the years he has had a lot of education and guidance to help him become a better cyclist, he told me. But when he first started his hobby, he was genuinely surprised by how complex such a simple looking pastime could be. Planning out routes, having the right clothing and kit, even making sure the tyre pressures are appropriate for the climate and terrain are all considerations.

Although the basic design of the bike hadn't changed in 100 years, the materials and supporting technology (for example, Satellite Navigation for bikes, online training programmes and forums) had.

He told me that he didn't realise how incompetent he was until he started to get some good quality education and guidance; and that is where I think the parallels are.

Pensions have been around for over 100 years, and at first glance they look pretty simple. Part of a salary or income is set aside and invested on behalf of an individual. Added to it might be further contributions from the employer and the government in the form of tax relief. With investment returns and dividends we hope that by the time we retire there will be a healthy source of income.

That bit is easy to understand, and until very recently employees had to give little thought to how this all happened. Freedom and choice has changed this dramatically. But are employees equipped with the knowledge to deal with it?

The problem here is that like cycling, what looks simple actually has a lot of complex elements to it. When you look at what goes into the mix to get to an income, assumptions about mortality, longevity, investment returns and considerations about tax and any other lifetime savings, it is a steep learning curve for an employee who might have had very little engagement with their pension over the years. And whilst the general options at retirement haven't changed (cash, annuity or drawdown), these options and how they can be used are new territory to many.

Research provides conflicting views of the mind-set of the UK's pension savers in this territory; some claiming the over 55s won't pay for advice as they feel they don't need it, some that shows that people are worried about making decisions about their retirement savings, whilst other research shows people are confident in their abilities to do so.

But what is evident is that scams appear to be on the rise, people are paying more tax than expected, and savers don't seem to understand their options as they face retirement. For instance, almost a quarter of people questioned in a Pensions and Lifetime Savings Association (PLSA) survey thought that there are no risks with drawing a regular income from their pension pot; something which is far from accurate.

At this early stage of pension freedoms, I believe these pension savers are in a state of 'unconscious incompetence'. That means that they are not fully aware of what they don't know, and are therefore at risk of making poor decisions, and getting less retirement income than they ought to. Financial education is a good antidote to this; our figures show that around 60% of employees who attended one of our retirement seminars will ask us for either help, guidance or advice following the seminar. I'm confident the figure would be higher if we counted enquiries back to employers, schemes, trustees, other advisers and Pension Wise.

I'm equally confident that if good quality education, guidance and advice services are made available by schemes and employers, then pension savers will get better outcomes in retirement.

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