expert insight

PMI EXPERT PARTNER

FINANCIAL EDUCATION

An allowance for advice

The Pension Advice Allowance (PAA) became available this April to help individuals pay for the cost of regulated financial advice for retirement.

The allowance enables individuals to withdraw £500 from their pensions, at any age and up to three times, but only once in a tax year. It is available to defined contribution (DC) pension savers, as well as 'hybrid' pension savers with a DC or cash balance element.

It's too early to say if it's been a success, but reports from some of the bigger schemes in the UK are stating there has been little or no uptake. This may be due to lack of public knowledge of the allowance, or because as previous research has shown numerous times, people just aren't willing to pay for financial advice. This reluctance, I believe, comes from individuals not understanding what financial advice is, or what it can do for them.

In contrast, when we look at the results of employees who have attended a pre-retirement education seminar in the workplace, around 60% go on to request further information and advice following a session. The difference is that following financial education, employees will realise how complicated pension decisions can be, and will gain an understanding of how financial advice can help them.

In fact, financial education and guidance delivered in an informative and meaningful way can have a real impact during the pension accumulation stage, without the need for employees to access their pensions to pay for advice. For example, one of our clients carried out research into employee behaviour post-education and guidance in the workplace. The results showed that following financial education, 40% of employees went on to increase their pension savings, and 20% increased their share plan contributions.

A cost issue?

Although the Treasury said there wouldn't be an impact on scheme members accessing their pension to pay for advice, taking £500 from a pension scheme – whether that is once, twice or three times – will no doubt have an impact on its end value. The earlier it is taken the bigger the impact, as the money taken will no longer have the opportunity to grow in value.

Indeed, higher figures than the £500 allowance were suggested in the consultation, but the Treasury believed that restricting it to this amount would spark innovation from financial advice providers to come up with cheaper or more automated ways of providing advice services for employees; in particular robo advice.

To date there are no robo services capable of assessing the complexities and range of lifetime savings that can be used to generate retirement income; or take into account taxation consequences and the risks inherent with income drawdown and other retirement strategies. I have no doubt there is a place for robo advice in making simple savings decisions – but not at-retirement.

But what is the alternative?

What many employees don't realise is that it's possible to receive financial advice on 'a try before you buy' basis without having to pay for it up-front, therefore keeping valuable savings in their pension to grow further, and then only paying if they decide to act on what is recommended.

With these models available it's hard to see why an employee would need to access their pension to pay for advice.

Workplace engagement is key

However innovative the service, the key to making sure that employees get the most of the money they've saved throughout their working lives is through engagement in the workplace.

Supporting employees with financial education and guidance will help them to make better decisions pre-retirement, without having to reduce the value of their pension savings unnecessarily. The benefit here is that employees save effectively and can afford to retire, something in both the employee and employer's interests.

This then drives the process of taking financial advice, ensuring that employees understand their personal financial situation, and are able to implement their retirement strategy in a tax-efficient way.

In conclusion, the jury is out on whether the PAA will be a success. Anything that provides options designed to lead to better outcomes for employees and pension scheme members is welcomed – but I believe the best results will arise from workplaces supporting employees with financial education, guidance and advice.

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WEALTH at work

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