PRESS RELEASE
FOR IMMEDIATE RELEASE
TUESDAY 28th SEPTEMBER 2010

"Government proposals to remove the requirement to annuitise pension saving could give people greater choice at retirement, but could expose them to increased risks" says Pensions Policy Institute

The Government has proposed to remove the effective requirement for individuals to annuitise their pension saving by the age of 75 to give people greater choice over how they can provide a retirement income for themselves. The Government is consulting on the details of its proposals and the PPI has today published its response to HM Treasury's consultation.

Niki Cleal, PPI Director, said:

"Converting pension saving into a retirement income is one of the most complex financial decisions that many individuals will face. The Government's proposed approach to removing the effective requirement to annuitise by age 75 would give people greater choice at retirement, but it could also pose significant risks to individual's retirement income if people are poorly advised or simply do not understand the implications of the choices that could be available to them."

"One of the main risks that individuals with small pension pots face is the risk that their pension fund is depleted before their death. An annuity provides a secure income until death and so provides an important guarantee that an individual will have an income throughout their lifetime. The Government will need to ensure that its new approach minimises the risks of individuals running out of income prematurely or from seeing the value of their retirement income eroded by high inflation or unexpected falls in the stock market."

In relation to the Government's proposals for a Minimum Income Requirement, Niki Cleal said:

"Many pensioners might be able to meet an MIR set at the Guarantee Credit level of £132.60 a week in 2010 for a 30-year retirement from their state pension income alone if they have a full Basic State Pension (£97.65 a week) and at least half of the maximum entitlement to additional state pension (£63.50 a week). However, this level of income will not be able to provide for most people's expectations of a comfortable retirement. "

"An individual with a full Basic State Pension (£97.65 a week) and the median amount of occupational pension (£104 a week) might be able to stay above an MIR set at the Pension Credit level of £183.90 per week in 2010 for a 30-year retirement by purchasing an RPI-linked annuity with £60,000, or by purchasing a level annuity with £85,000, although the Government is currently intending to require people to purchase an escalating annuity to satisfy the MIR."

"If the Government were to introduce an MIR that reduced the risk of people falling back onto Guarantee Credit, Pension Credit and average levels of Council Tax or Housing Benefit, then the MIR would need to be set at a high level of £596.20 per week in 2010. An individual with a full Basic State Pension (£97.65 a week) and the median amount of occupational pension income (£104 a week) would need to purchase an RPI-linked annuity with £880,000 to meet an MIR at this level. Very few individuals are likely to be able to satisfy such an MIR."

"What these numbers reflect is that while it might be realistic to set an MIR at a level that stops people from falling back onto means tested retirement benefits including Guarantee Credit and Pension Credit, to stop people falling back on other means tested benefits is going to limit the number of people who could meet the MIR to very few individuals."

ENDS

NOTE: This document is based on the PPI's response to proposals contained in a Government consultation. The Government has not yet announced the details of its final approach.

The PPI's evidence is intended as a contribution to the policy debate. Nothing contained in this document is intended to constitute financial advice and should not be used by individuals as the basis for any financial decision making.

Notes for editors

1. The Pensions Policy Institute is an educational charity, which provides non-political, independent comment and analysis on policy on pensions and retirement income provision in the UK. Its aim is to improve the information and understanding about pensions policy and retirement income provision through research and analysis, discussion and publication.

2. The Government has proposed to lift the effective requirement for individuals to annuitise their pension saving by the age of 75 to make pension saving more attractive by giving individuals greater choice over how they can provide a retirement income for themselves. The Government has proposed an alternative approach that would allow individuals over age 55 to:-
   - purchase an annuity;
   - to invest their pension savings in an income drawdown arrangement with a cap on the maximum allowed withdrawal, (capped drawdown); or,
   - to withdraw unlimited amounts from their pension saving, provided that individuals can demonstrate that they have met a minimum income requirement (MIR) to prevent them from falling back onto the state (flexible drawdown).

3. The Government is consulting on the detail of how the new approach might work. The PPI has submitted the evidence that it considers relevant to the Government's consultation and focuses especially on the trade-offs between risks and flexibilities for individuals that could result from the new approach.

4. The Government has proposed to introduce a Minimum Income Requirement (MIR) that would enable individuals to withdraw unlimited amounts from their pension fund if they can demonstrate that they have sufficient resources that they are unlikely to fall back onto the State. The MIR could be calculated using several different levels of entitlement to means-tested benefits, or it could also be set in relation to other measures of retirement income.

5. If the Government wished to set the MIR at a level which would reduce the likelihood of people falling back onto the Guarantee Credit element of Pension Credit, then the could MIR would need to be set at or above the current Guarantee Credit Level of £132.60 per week in 2010.

6. If the Government wishes to set the MIR at a level which would keep people off both elements of Pension Credit (Guarantee Credit + Savings Credit), then they could set the MIR at the minimum income level above which people are no longer eligible for Pension Credit, £183.90 per week in 2010.

7. If the Government wished to set the MIR at a level that is likely to keep people off Pension Credit and average levels of Council Tax Benefit and Housing Benefit then the MIR would need to be substantially higher, at £596.20 per week in 2010.

8. Table 1 below shows the size of annuity that would be needed to satisfy an MIR set at these alternative levels. The Government proposes that state pension income from the Basic State Pension and the State Second Pension and Occupational Pensions with limited price indexation would all currently count towards the MIR. The Government has not proposed to include income from level annuities, however the PPI has included this in our illustrative analysis.

Table 1: Size of annuity purchase required to meet a Minimum Income Requirement set at three different levels of means-tested benefit entitlement for 30 years given different levels of eligibility to state pension and occupational pension

Level of BSP and S2P[1]	Guarantee Credit[2]		Pension Credit[3] (Guarantee Credit + Savings Credit)		Pension Credit + Average Housing & Council Tax Benefit[4]	
	Required weekly income **2010:** £132.60		Required weekly income **2010:** £183.90		Required weekly income **2010:** £596.20	
	RPI-linked annuity[5]	Level annuity[6]	RPI-linked annuity	Level annuity	RPI-linked annuity	Level annuity
Full BSP (£97.65) ½ S2P (£63.50)	£0	£0	£100,000	£145,000	£920,000	£1,355,000
Full BSP(£97.65) Occupational Pension (£104)[7]	£0	£0	£60,000	£85,000	£880,000	£1,295,000

[1] BSP increased by greater of earnings, CPI or 2.5%, S2P increased by CPI
[2] Uprated by earnings
[3] Guarantee Credit element is uprated by earnings, Savings Credit is assumed to rise with earnings until 2015, after which it is frozen in real terms
[4] Eligible rent levels for Housing Benefit rise in line with average rents, and then in line with CPI from 2013/14, Incomes above eligibility for highest rate of Housing Benefit are assumed to be above eligibility for Council Tax benefit
[5] Based on best available annuity from FSA tables as of 2nd August 2010 - an individual with £100,000 would receive an income of £6,408 per year from a level, single-life annuity
[6] Based on best available annuity from FSA tables as of 2nd August 2010 - an individual with £100,000 would receive an income of £4,032 per year from an RPI-linked annuity
[7] Median receipt

Notes on Table 1

- Table 1 shows the level of savings an individual would require to purchase an annuity which could keep them above hypothetical MIR levels for 30 years.
- The MIR levels are calculated using income levels above which people are no longer entitled for specific means–tested benefits: Guarantee Credit, Pension Credit, Pension Credit + average levels of Housing and Council Tax Benefit.
- The Government re-evaluates the maximum amount claimable for each means-tested benefit annually. The calculations assume that the Government's current indexation or uprating policy for each means-tested benefit continues in the future. For example, Guarantee Credit is currently indexed in line with average earnings and in the calculations we have assumed that this continues to be the case in the future.
- The calculations assume that price and earnings inflation continues at expected levels.
- All annuity purchase figures are rounded to the nearest £5,000.
- ½ S2P refers to half the current maximum level of entitlement for additional state pension of £63.50 a week. Additional state pension includes entitlements to the State Earnings Related Pension (SERPs) and the State Second Pension and predecessor schemes.

9. These calculations are not recommendations of the appropriate level of MIR, they are merely hypothetical examples of where the Government could set an MIR designed to keep people off means-tested benefits. For example, Table 1 shows that if the Government were to set the MIR at the level of the Guarantee Credit of £132.60 per week in 2010, then individuals with a full Basic State Pension (£97.65) and half of the maximum possible eligibility to additional state pension (£63.50) would be able to meet this MIR from their state pension income alone.

10. However, if the Government set the MIR at the level required to reduce the likelihood of individuals falling back on to Pension Credit then the MIR would need to be set at £183.90 per week in 2010. An individual with a full Basic State Pension (£97.65) and half of the maximum possible eligibility additional state pension (£63.50) would be able to meet an MIR of £183.90 a week by purchasing an RPI-linked annuity with £100,000 or a level annuity with £145,000. An individual with a full Basic State Pension and the median amount of occupational pension (£104 a week) would need to purchase an RPI-linked annuity of £60,000 or a level annuity with £85,000 to meet this MIR.

11. If the Government set the MIR at the level required to reduce the likelihood of individuals falling back on to Pension Credit, or average levels of Council Tax Benefit or Housing Benefit then the MIR would need to be set much higher at £596.20 per week in 2010. Very few individuals are likely to be able to meet an MIR set at this level. An individual with a Full Basic State Pension and the median amount of occupational pension

income (£104 a week) would need to purchase an RPI-linked annuity of £880,000 or a level annuity of £1.3 million to meet an MIR set at this level.

12. The PPI is currently conducting further research on this topic as part of its *retirement income and assets* research series. The retirement income and assets series has considered what determines individuals' needs for retirement income and has examined the role that state, private pensions, housing and other financial assets can play in meeting those needs for retirement income. The PPI is grateful to all of the sponsors of this research series.

13. The forthcoming PPI report in the series explores the implications of lifting the effective requirement to annuitise by age 75 and considers the possible impact of the Government's proposal as well as other policy alternatives on individuals, industry and the Government. All of the reports in the retirement income and assets series can be downloaded from the PPI website at www.pensionspolicyinstitute.org.uk.

For further information please contact -
Niki Cleal, PPI Director on 020 7848 3744 or 07834 275083
email: niki@pensionspolicyinstitute.org.uk

Martin Campbell, Beacon Strategic Communications: 07802 634695
email: martin@beaconstrategic.com