Why drawdown should be an advised option

Drawdown is an incredibly complex – and important - part of a retirement strategy. That being the case, should the FCA apply the same rules to drawdown as they currently do for DB transfers and pension benefits that have guarantees attached? Essentially, whenever the pension transfer or drawdown investment exceeds £30,000, should professional advice be mandatory?

When you consider the extent of the information required and the decisions to be made there appears to be a strong case for mandatory advice. The list below is not exhaustive and more questions will doubtless arise after the initial answers. Failing to carefully consider and fully understand all the options and risks involved can and is likely to result in poor and in some cases disastrous outcomes.

<u>Key questions to consider before adopting a suitable drawdown strategy</u>

- What are the clients objectives from the pension arrangement, for example, is it for holistic planning, tax mitigation supporting an existing lifestyle, or as simple as paying for basic living costs?
- What are the basic living costs and how will these be met if drawdown income runs out?
- Is income required immediately or at some time in the future?
- Is tax free cash required now and, if so, is it all or part?
- Do they need guaranteed income or income provided through investing?
- What level of income required and will this increase or reduce?
- If there's other retirement income and capital available (outside the pension arrangement) – how accessible should it be?
- Is downsizing or equity release an option later in retirement?
- Who, other than the member, may be dependent on the pension income?
- Are there any health issues and what is the expected longevity?
- What is their risk profile and capacity for loss?
- What investment strategy is preferred?

Depending on the answers given, suitable options (with advice) may be very limited - but will the DIY investor ignore the inherent risks of drawdown, and focus only on the key objective of obtaining the highest income available? In this scenario drawdown is likely to seem far more attractive than the other retirement options available.

Choosing the most suitable investment strategy is only one factor in the decision but will probably present a major challenge, especially for the novice investor. A range of online tools is available to support them, however, when the individual's main focus is on maximising income the tool may highlight specific risks but there is nothing to stop the DIY investor proceeding. Given the added complexity of drawdown in simply making a straight forward investment, the tools associated with selecting the most appropriate funds may be inadequate.

There are of course specific risks for individuals opting for drawdown. Hopefully with professional advice these risks are discussed and clearly understood, but the DIY investor is unlikely to be aware of them all.

These include:

- Withdrawing unsustainable levels of income and prematurely depleting fund.
- Living longer than anticipated and running out of income.
- The sequential risk of investing and withdrawing when markets are falling and using other sources of income to mitigate these events.
- Making poor investment choices that may not be aligned to risk profiles or meeting the key objectives of delivering a stable regular income.
- Withdrawing funds in an inefficient tax manner – not using tax free cash etc.
- Inappropriate fund switching.
- Not making or updating death benefit preferences.
- Ignoring the ongoing option to annuitize when it may be most advantageous to do so, for example if health declines and or interest rates rise.

Now, more than three years on from the introduction of Pension Freedoms, how many non-advised cases will result in poor outcomes?

It's probably too early to tell – many savers with small saving pots have already withdrawn their entire funds from a drawdown and are probably comfortable in the decisions they made. But do we know about those with significantly larger pots who are seeing their funds deplete much quicker than anticipated? After all, complaining (having not sought professional advice) is unlikely to change matters, and in any case will future surveys pick up these poor outcomes?

There is a bright spot, as recent press stories show more advisers seem prepared to give advice to clients who have modest saving pots than back in 2015 and 2016. This would suggest that advisers are more comfortable taking on clients in these situations now the regulations have bedded down.

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