

Delivering the pension message

– is it getting through?



Kevin Fitzsimons, Pension Product Manager, Irish Life

Communicating the benefits of funding a private pension has always been challenging and none more so, than in recent years, with decades of legislative changes. Lack of affordability is often not the sole reason people don't fund a pension adequately. I believe the voluntary pensions system, and its incentives work perfectly fine, for those who chose to make the most of it, but the system is far from user friendly, and undoubtedly has unnecessary layers of complexities. Until such time as a simpler process is introduced, the challenge for the industry is to always communicate the benefits on offer from that system, in an effective manner. And yes, this is far easier said than done.

Adding to the challenge is the fact that clients can be confused, and misled by one sided or even misinformed media reports on pensions. However, if we really believe we have the ideal 'no brainer' solution to a client's worry of not having enough to live on in retirement, as I believe we do, why are more clients not availing of it, and why does the pensions coverage gap remain so stubbornly high?

When public sector employees are taken out of the equation, only around 40% of employees have personal or occupational pension arrangements. We also know that personal money on deposit with financial institutions is significant, so is it the case that many people with no pensions, opt instead, to leave 'after tax' money on deposit for the medium to long term, with such money barely keeping pace with inflation, not to mention attracting a 41% DIRT tax rate on minuscule returns. It just doesn't make financial sense (Source: Is Ireland's population ready for retirement? McKinsey & Co. 2015).

Now, having a rainy day, or emergency fund that is liquid, and has quick and easy access, should be part of prudent financial planning for everyone. However, for approximately 60% of the private sector working population, to ignore a whole series of tax breaks designed by Government to give clients a more comfortable retirement or possibly to help those clients even prosper in retirement, points in my opinion, to a clear communications deficit in the pensions industry.

Pensions are too complicated but don't have to be.

Some people according to regular industry surveys, view pensions as being too complicated, and who in the industry would dispute this? However, when you boil it all down, a pension need be no more complicated than a fund you contribute to over your working lifetime, the proceeds of which you live on, when you retire. Except you enjoy a significant tax break from the beginning of the process, in the form of contributions attracting tax relief, a tax break in the middle of the process, in the form of tax free returns, and you enjoy two tax breaks at the end of the process, when you draw down benefits. These last two tax benefits take the form of a tax efficient retirement lump sum, as well as the ability to engage in tax planning on income drawdown from an Approved Minimum Retirement Fund (AMRF), and Approved Retirement Funds (ARFs), if the scheme is Defined Contribution in nature.

Let me try for one moment, to put the value of income tax relief in context. And, as I say, it's important client's appreciate that the tax relief is only one tax benefit in the process.

- Income tax relief at 40% represents an immediate uplift to your money of 66%
- It represents a 25% uplift, if you are entitled to standard rate income tax relief.
 - * (note that pensions are taxable in payment)
 - * An immediate uplift of 66% or 25% on your money is actually the equivalent of a compounded return on your money of 2.5% over 21 years and 10 years respectively.
 - * So, a 40% income tax break is the equivalent of 21 years of 2.5% net returns upfront!

Most people are lucky to receive 1% deposit rates these days, on their hard earned 'after tax' money, and even that is subject to 41% DIRT tax. **If 40% income tax relief was translated into a 1% tax free, net, compounded return on your money, you would need over 50 years of such returns, just to equate to the 40% tax relief, you would receive instantly on your money through funding a private pension. And that's just the first contribution!** It's a sobering thought, but I wonder how many clients realise this. Pensions are of course taxable at marginal rate tax in payment, but this can sometimes be minimised depending on overall income in retirement.

So how should we position pension products?

So sometimes we need to take time to 'sharpen the saw' as author Stephen Covey says in his book 'The Seven Habits of Highly Effective People', and reflect on how we position pension products, and how we communicate key messages. We should ask ourselves some searching questions.

- Could our sales pitch or pension presentation, which we use with new and existing clients be improved?
- Is the pitch fit for purpose in 2016?
- Do client's 'get' just how tax efficient pensions are, and how the taxman can actually contribute to their wealth, via a pension?

Most clients research pensions these days, before they ever go face to face with a financial or pensions advisor. It is however, a notoriously difficult subject for a layperson to research and the value of the financial advisor helping the client to navigate the system, and communicating key messages is obvious. Many clients also fail to recognise the tax treatment that often applies to any gains, growth or income on private investments, following on from a series of recessionary budgets. And some even fail to recognise that many of these private investments are made from 'after tax' income to begin with?

Pension funding despite recent restrictions, limits and caps is arguably as attractive now, as it was ten years ago, before the economic crash (with the exception of the €2 million lifetime cap and €200,000 cap on tax free cash) and far more attractive than 20 years ago, when annuities were the only post retirement products available. Pensions deserve to be revisited by clients with the guidance of their financial advisors. **What a tragedy it would be for clients to ignore, for whatever reason, such a valuable package of tax benefits, designed to make retirement comfortable, and to maintain their pre-retirement standard of living.** Sadly, the often quoted pension coverage statistics would suggest many do ignore it.

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