August 2020

Centralised Retirement Propositions

Creating your framework

ascentric

For investment professionals only

Introduction

There's been an increase in regulatory scrutiny of the suitability of retirement advice and we only expect this to intensify. This is a key reason why financial advice firms are focusing on having a rigorous approach to advice for clients in retirement.

A centralised retirement proposition (CRP) is one way of establishing and agreeing an approach to advice.

It can also prove an invaluable tool to help reassure clients during times of market volatility and investor uncertainty.

We asked research specialists NextWealth to carry out an extensive survey of 200 firms, including many who've implemented a CRP. We explored the ways they define a CRP, their rationale and approaches to adopting one and the component tools they use. We interviewed a number of planners in depth to find out how they believe CRPs can benefit both their business and their clients.

We've created this guide to walk through some of the key findings in our research. It has highlighted that planners have a wide range of experience and advice firms have different levels of process in place.

We hope that this guide will give you some food for thought, if you or your firm are considering implementing a centrally agreed approach to retirement planning.

Each firm and its clients are different; so you're best placed to create a suitable solution for your clients and your business. But as a starter we examine six key considerations when introducing a CRP and outline seven steps that can help establish a plan. And we've turned these into a checklist to run through when documenting your CRP.

Six key questions to consider

1. Should the firm have an agreed framework for retirement advice?
2. What components should a CRP include?
3. What tools are needed to support the CRP?
4. How do I turn assets into income?
5. How should the firm assess the sustainability of withdrawals?
6. What is the scope of the CRP?

Six Questions

The responses and more in-depth discussions with planners during our research drew out some interesting and practical examples that defined these considerations.

1.

Should the firm have an agreed framework for retirement advice?

Here are some of the main reasons planners gave for introducing a framework for retirement advice:

> “We have a large proportion of clients starting to reduce their hours at work, taking income from retirement, combined with a lot more people going into unsecure income, flexi access drawdown, less annuities. Clients running out of money is a real risk, therefore shouldn’t we have an additional process to make sure we’re consistently challenging our advice to make sure it is still appropriate by various metrics?”

> “We have a wave of people in retirement, leaving money invested because they don’t want to buy an annuity, so what are their issues and concerns? Shouldn’t a professional firm put a process together to manage clients’ spending? Gives us more of an edge on what we do for clients.”

> “We’ve just drafted our first stab at a CRP. The old model we had didn’t seem fit for purpose. If a client saw 3 different advisers, they’d get 3 different outcomes. A large part of the motivation is de-risking, but also just bringing down the admin time and paper trail and being more efficient.”

Reducing business risk is an important driver, but firms are not moving to a CRP as a “box-ticking response for the FCA”, as one principal told us. They’re making a positive choice to introduce a consistent and centrally agreed approach to planning in retirement.

Benefits of a CRP

- **Better service to clients**
- **Better business efficiency**
- **Reduce business risk**

• Better service to clients

The number one benefit quoted by firms who implemented a CRP is client benefit. With a CRP in place, the firm is able to offer consistency across its entire client bank, with a clear and agreed framework for retirement planning. They can communicate the process to new and potential clients as a positive and structured approach to dealing with a complex and confusing issue. They can present a professional, written policy on managing sustainability of withdrawals to assist with client conversations and mitigate against the risk of clients running out of money in retirement.

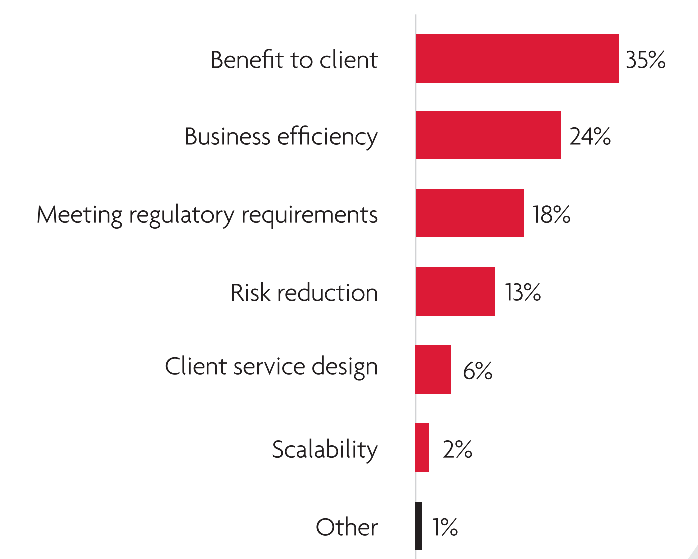
• Better business efficiency

As one planner said, a CRP brings “a consistent approach that makes life a lot easier.” More commonality means processes, paperwork and operations may be more streamlined.

• Reduce business risk

Having a CRP means “one less headache”, according to one of our interviewees. It represents a clear and demonstrable process that’s followed across the firm regardless of which planner a client meets with. And, like a centralised investment proposition (CIP) it gives firms consistency and better governance of their investment recommendations.

Greatest Benefit of a CRP



Source: Ascentric/ NextWealth survey, all planners whose firms has a CRP in place or intend to introduce one, n=144

60% of firms currently have a centralised investment proposition in place

2.

What components should a CRP include?

According to our research, 60% of firms currently have a centralised investment proposition in place, increasing to 78% for firms with more than five planners.

It might seem an easy win to take an existing CIP and tweak it for retirement advice. However, our conversations with firms who've successfully adopted a CRP reveal that the CRP should extend beyond investments to include financial planning aspects of retirement advice.

> "It's not a case of taking a CIP and change the funds to income-oriented funds and there's your CRP. Concentrate on the process and framework and less on the investment bit. How do you get to those outcomes?"

Client segmentation

With the introduction of MiFID II and PROD 3.3, advice firms are now being asked to be clear about the categories of clients they serve and the products and services that are suitable or not suitable for them. Some firms have found the segmentation exercise useful as a way to bring consistency to the business and ensure they are offering a comparable service to clients with similar needs.

Our research found that most financial advisers segment clients based on level of investable assets. Only one third segment clients based on lifestage. Most regulatory experts suggest that client segmentation based on assets is insufficient. It is unlikely the needs of a 35-year-old who inherits £500k will have the same needs as someone planning to retire aged 60 with the same level of assets. Client segments can be used to tailor the service and support offered to clients and best practice is to use a matrix approach taking in to account a number of factors like client lifestage, complexity of requirements, platform and service level.

Aspects of retirement planning

For retirement clients, even more so than those in the accumulation phase, the firm's centrally agreed process should focus on individual suitability and planning elements like: understanding the client's objectives and expectations, developing a sustainable withdrawal strategy, assessing ability to bear loss, and looking at the investment horizon through longevity assessment. The wider context including the client's intentions and wishes around intergenerational wealth transfer and estate planning needs should also be taken into account. 59% of planners we surveyed consider intergenerational wealth transfer a core part of the service they offer to retired clients.

Retirement planning involves many unknowns. Most people don't know when they will retire, how markets will perform or when they will die. While this drives up demand for professional financial advice, it puts a lot of pressure on financial planners. One interviewee said "it's the scariest thing we do" when we asked about the complexity of retirement advice.

Longevity assessment

One of the great unknowns in retirement planning is longevity: how long a client will live. We found little evidence of advice firms using a scientific approach to assessing longevity. 16% of planners we surveyed use the average life expectancy figures given by Office for National Statistics (ONS) data. Currently only 2% of advisers engage an underwriting service to assess longevity of retirement clients. This type of assessment typically involves a medical assessment and an adjustment of the ONS longevity estimate to incorporate specific health and lifestyle factors, producing a more detailed and objective assessment to base retirement planning decisions on. More could be done to assess longevity to minimise the risk that a client will either run out of money or underspend during his or her lifetime.

Vulnerable clients

Finally, the transition into retirement represents a major life change for clients and compounds the moments when clients can potentially be vulnerable. The vast majority of planners who responded to our survey have dealt with vulnerable clients. One said: "everyone entering retirement is vulnerable to some extent," underscoring the scale of the challenge. So, good practice would also be to include a centrally agreed approach for dealing with vulnerable clients as part of the CRP. The most common approach used by the firms we surveyed is to ask for a friend or family member to be present in conversations. The CRP should reference the firm's process for identifying and dealing with vulnerable clients.

Six Questions

3.

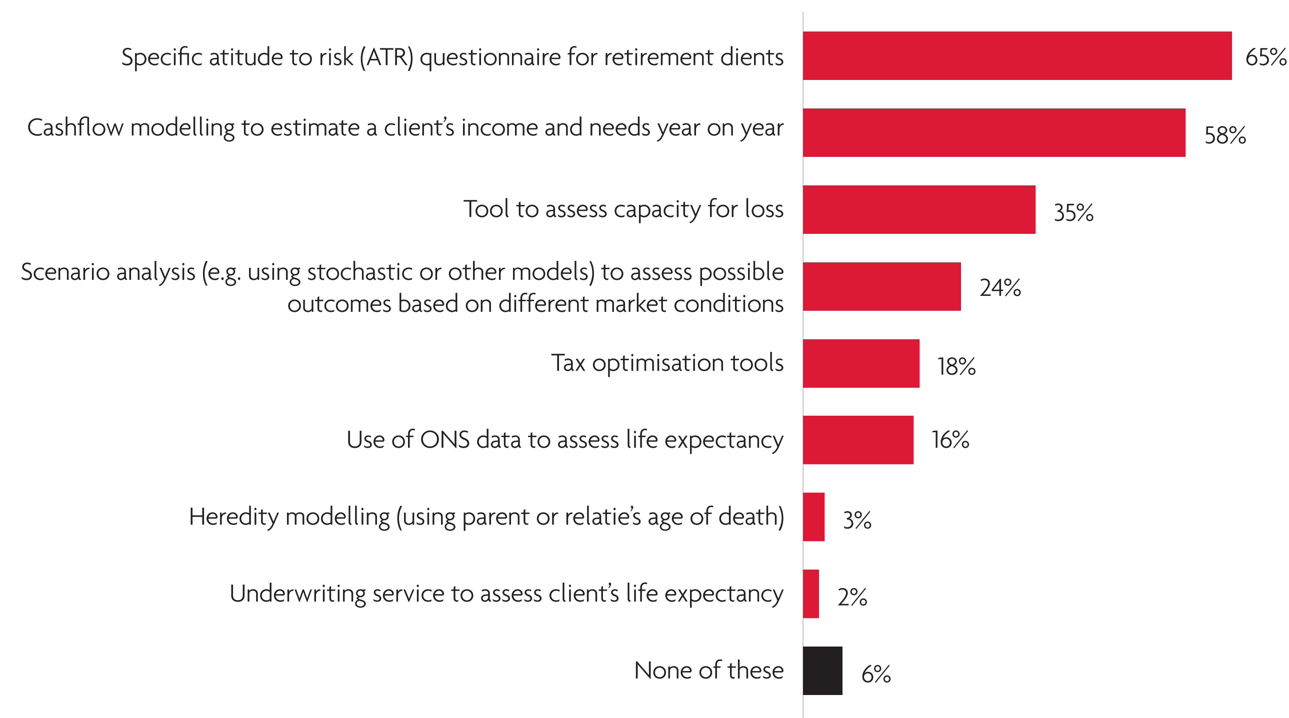
What tools are needed to support the CRP?

For some firms, the retirement proposition is built around the use of particular tools, especially cashflow modelling.

Our research among firms currently with a CRP show a specific attitude to risk questionnaire for retirement clients is the most common element of the proposition.

Cashflow modelling and tools to assess capacity for loss also feature heavily.

Tools used within a CRP



Source: Ascentric/NextWealth survey, all planners who have a CRP, n=97

To see the full finding of our research on Centralised Retirement Propositions visit **our website to download a copy**

4.

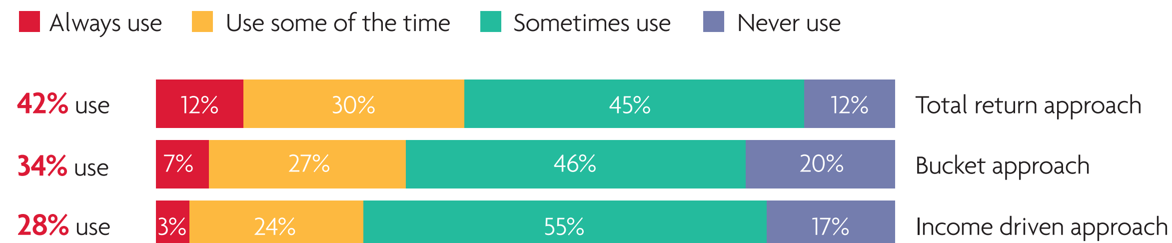
How do I turn assets into income?

This question is as relevant for your straightforward drawdown clients, as it is for complex, tax planning scenarios, in a multi wrapper retirement.

Since pension freedoms an annuity is not the only answer. But, your core 'go to' solution will probably be influenced by your knowledge and experience, how you view the best way to mitigate risk and the makeup of your client bank.

The research found that the most popular method for managing income with 42%, was to run the portfolio on a total return basis. Next, with 34%, was the bucket approach. And finally, with 28%, was an income driven method. All could be suitable solutions, but it's never a one-size-fits-all and more often than not, it's a combination of several approaches.

Portfolio construction for those taking retirement income



A fully invested portfolio has the greatest chance of providing a sustainable income

Total return

The total return approach is favoured by probability-based advocates. Stochastic modelling seems to indicate that a fully invested portfolio has the greatest chance of providing a sustainable income that could last for the rest of the client's life.

Bucket

But then there's managing client behaviour and the challenges associated with helping them stay the course during volatile times. Proponents of the bucket approach might feel total return is too much of a white-knuckle ride for their clients. They may like dividing the client's funds into long, medium and short-term pots so the client can mentally account for where their income is coming from. And, the different risks they're taking.

This could remove some of their worry; but, even if you simplify this into an invested and cash buffer approach, you need to address the cash drag issue.

Natural income

The income approach is the least popular. Probably because finding a client who has sufficient assets to live off their income, who can live with the unpredictable amount of income and who can accept that their capital isn't 100% secured, is probably part of a much smaller segment.

What next:

Recognise and manage your biases – and the biases inherent in your processes – when identifying the most effective income strategy for clients. Just outlining the options in a documented CRP can help.

Your core income solution is core for a good reason. Think about how you can effectively and efficiently manage the outlier clients. DFMs that work on platform can be a great option for complex clients where you're trying to juggle issues like managing CGT out of assets, complex income requirements, strong ethical / ESG positions, combining income and legacy planning with IHT efficient assets, and many more.

Finally, when you think of your CRP and how you articulate meeting the clients income needs, start with the basics. How, if possible, securing their must-pay bills through a guaranteed income could give them a secure base to invest from.

5.

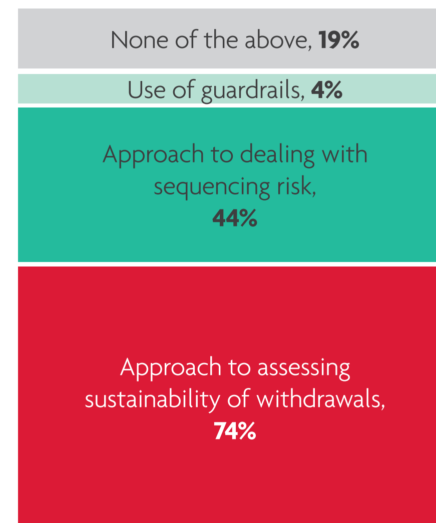
How should the firm assess the sustainability of withdrawals?

Withdrawal strategy is central to the CRP and can have at least as much, if not more, impact on the sustainability of income to clients in retirement.

Most advice firms include a centrally agreed approach to assessing the sustainability of withdrawals as part of the CRP and nearly half also include a consistent approach to dealing with sequencing risk.

> CRP doesn't mean anything to the client; often they're still active, no one is properly retired so we call it our Withdrawal Policy Statement. You're spending capital; what's a safe way to do that? We built our own internal document which we update annually and share with the client.

Inclusion of a consistent strategy on client withdrawals



Source: Ascentric/NextWealth survey, all planners who have a CRP, n=97

One of the planners we interviewed uses FinalytiQ's Timeline tool to assess sustainability, finding that it puts clients in a more informed position. Another firm created their own traffic light system and a report for clients to show how the current withdrawal rate is affecting income projections.

Agreeing a consistent, firm-wide approach to determining a sustainable withdrawal rate is crucial. In the past many planners relied on the 4% rule but this approach has been mostly discarded as too simplistic and not reflective of the various portfolio risk levels. Planners recognise that income needs will fluctuate throughout retirement requiring sophisticated modelling and ongoing planning support. This modelling should also take into consideration sequencing risk.

6.

What is the scope of the CRP?

We deliberately refer to the Centralised Retirement Proposition as a framework rather than a blueprint. The intention is to settle on the firm's best idea for its approach to due diligence, fact-finding, client assessment and retirement strategy, whilst retaining the flexibility to provide an investment solution that best fits each individual client and their circumstances and goals.

Most planners who have decided not to have a CRP say their main reason is their preference to tailor advice to each individual client. However, a CRP framework can absolutely accommodate this flexibility, while still allowing for a more process-driven, streamlined and repeatable approach across the firm.

In practice, only a fifth of our survey respondents whose firm has a CRP in place reported that they never go outside its scope. Nearly 30% say they look at bespoke solutions for clients at least once a month, and another quarter go outside the CRP a couple of times a year on average. This illustrates that the CRP is a workable solution for the vast majority of clients, and even if a bespoke investment solution is required then the rest of the retirement planning process can still hold true.

The majority of firms with a CRP that we interviewed have a sign-off process that requires planners to present a reason if they wish to go outside the CRP for a particular client. This allows the firm to monitor activity and maintain consistency and good governance.

A 7-point plan for introducing a CRP

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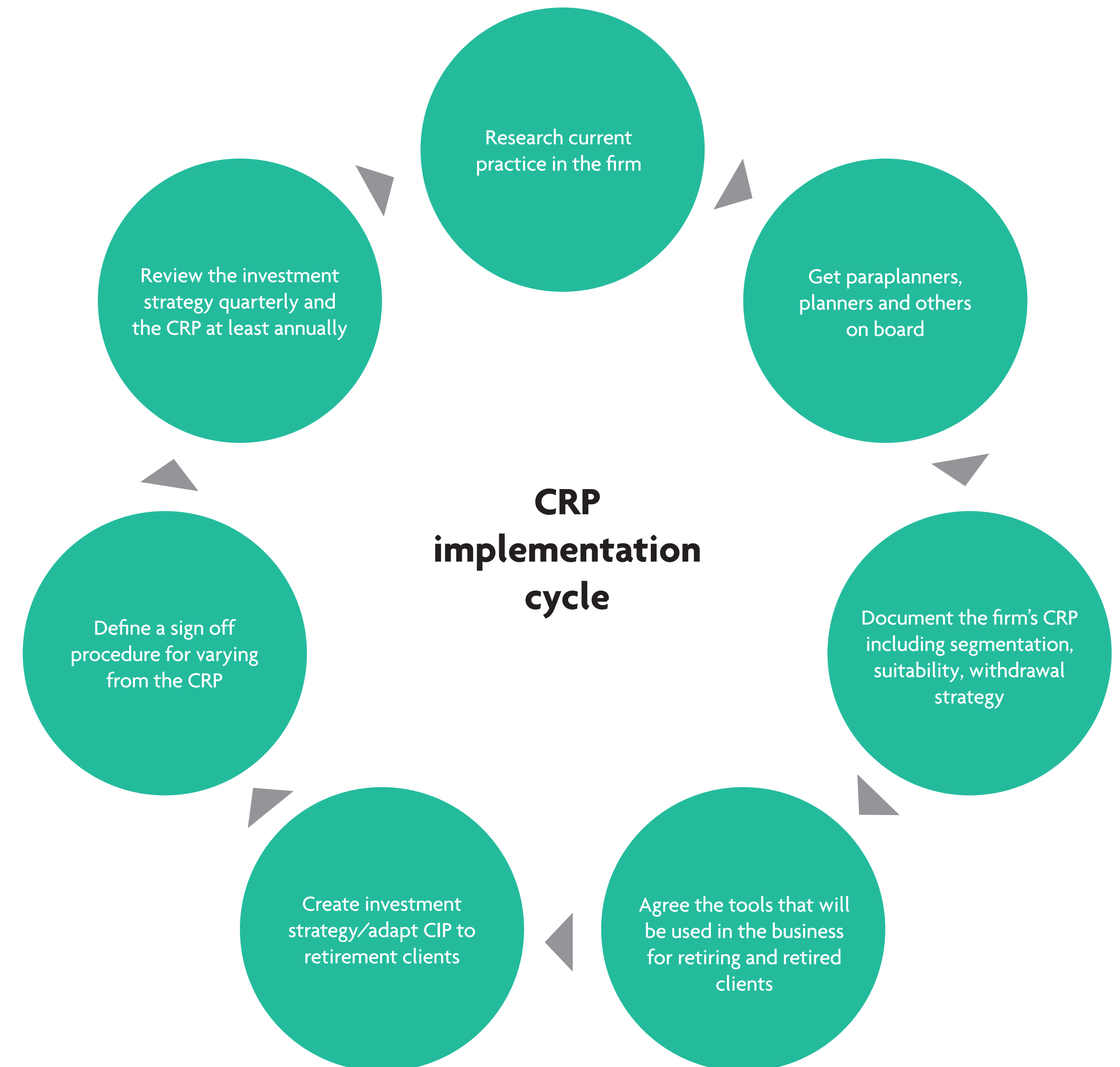
- **Do your research:** look at all the processes used in the firm for retirement clients, how they are used by planners and how they are presented to clients. Where will the firm and clients benefit from a standardised approach?
- **Get everyone in the firm on board:** if the firm has two or more client-facing planners, it's best to have them on the journey from the start and bought into the process.
- **Components:** document the firm's approach to client segmentation, fact-finding, suitability assessment and withdrawal strategy.
- **Tools:** what tools or systems are needed to support the CRP? Does the firm need to buy in tools, or are there tools already available in the firm but not currently fully utilised by all planners?
- **Investment strategy:** an existing CIP can be adapted for retirement or a new strategy can be created which could include converting to income generating share classes, use of cash buffers, instances when an annuity should be considered, etc.
- **Sign-off process:** develop a clear approach to making recommendations outside the CRP. This isn't to restrict the activity it's just to document it correctly.
- **Review process:** evaluate the CRP at regular intervals. Speak to key clients and get their feedback on what works for them.



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