



WHAT ARE THE ALTERNATIVES TO AN ANNUITY?

For those seeking a regular, predictable income, an annuity can offer peace of mind. However, under the new rules, you are no longer obliged to buy an annuity. Instead, there is a range of options to consider, either on their own or blended together to suit your personal circumstances.

● WITHDRAW YOUR ENTIRE PENSION POT AS CASH IN A SINGLE TRANSACTION

Theoretically, this offers you huge flexibility: you can withdraw all your pension savings, and use them as you wish. However, this strategy should be carefully considered; a bad or reckless decision could leave you in dire straits. Moreover, 25% of each withdrawal from your pension pot is free of tax, so you will have to pay income tax on the balance of 75%, and this could land you with a huge tax bill.

● LEAVE YOUR PENSION POT INTACT UNTIL A LATER DATE

This gives your savings additional time to grow; however, because your pension pot remains invested, its value has the scope to fall as well as rise. Nevertheless, by leaving your money untouched, you could buy an annuity at a later date and possibly benefit from an "enhanced annuity" if your health deteriorates in the meantime.

● WITHDRAW LUMP SUMS AS AND WHEN YOU WISH

You can choose how much to withdraw from your pension pot, and when (subject to your pension provider's rules). This option also provides considerable flexibility; however, there are caveats. First and foremost: you could run out of money. Moreover, although it allows you to spread your 25% tax-free allowance over a period of time, you need to take care that your withdrawals do not accidentally push you into a higher income-tax bracket. Furthermore, your pension provider could limit the number of withdrawals you can make during any one year, and your withdrawals might also incur charges.

● FLEXI-ACCESS DRAWDOWN

Flexi-access drawdown enables you to take up to 25% of your pension pot without paying any tax; the balance is invested to produce a regular, taxable income stream. Unlike an annuity, this income is not guaranteed. You can also dip into your pension pot when you choose (as long as your pension provider permits this), taking 25% of each withdrawal tax-free and paying income tax on the rest of the sum withdrawn. However, you should be vigilant as you could drain your pension pot over time.

Whatever your thoughts, to ensure you take account of the full range of available options, we would recommend you consider obtaining professional financial advice.

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We hope you found the information in this guide useful and informative. If any of the points are of interest, or you would like to discuss your own situation in more detail, please do get in touch.

Produced by adviser-hub.co.uk on behalf of your professional adviser.

This guide is intended to provide information only and reflects our understanding of legislation at the time of writing. Before you make any decision, we suggest you take professional financial advice. June 2020.

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GUIDE TO ANNUITIES

It takes many years of planning, saving and sacrifice to build up a significant pension – and, after all those years, you want to be sure you are making the most of it.

This guide is designed to provide you with the basic information you need to start thinking about your retirement opportunities. It cannot make any recommendations or decisions for you but, armed with the information it provides, you can start to ask questions and, with our help, make sure your retirement is as well funded as possible.

● WHAT IS AN ANNUITY?

An annuity is a regular fixed income that you buy with a lump sum. Its term may end at a fixed date in the future when you die or when another named person dies. The most common reason for buying an annuity is retirement, when you can choose to use part or all of the lump sum you have built up over the years through a company or private pension scheme to buy an annuity, thereby providing you with a lifetime's income. However, annuities can be bought with a cash lump sum from any source by any person who requires income.

● WHAT ARE THE CURRENT RETIREMENT RULES?

It used to be compulsory to purchase an annuity at retirement. However, following sweeping reforms to the pensions system that were implemented in April 2015, you can decide how to use your pension pot to suit your own personal circumstances. If you think an annuity might form part of your retirement plans, this guide provides an outline of the basic points, and a visit to your professional adviser will help you consider each in more detail.

● WHAT ARE THE BENEFITS OF AN ANNUITY?

On the one hand, an annuity offers peace of mind: you receive a regular, guaranteed income, either for life or for a fixed term. There is also a relatively wide choice available: for example, some annuities offer protection against inflation. Annuities can provide an income just for you, or for yourself and a spouse or partner, and can provide an income for them after your death.

On the other hand, when annuity rates are low, they do not necessarily represent good value. Therefore, it's crucial to take advice and shop around for the best deal.



BUYING AN ANNUITY

THE PROCESS

The first and most important question you have to ask is whether you want to buy an annuity at all. A number of alternatives are outlined overleaf.

Always remember that, once you have purchased a specific annuity, you cannot go back on your choice, so it is important to get that decision right. Annuity rates will change with the interest rate climate so, for example, if you are buying at a time when interest rates are particularly low, you may decide not to invest your whole retirement fund immediately and retain some of it instead.

In addition, when considering whether to buy that annuity, remember doing so will consolidate the value of your investment – unless you buy an investment-linked annuity, there is no possibility of benefiting from future growth. In addition, unless you write in certain guarantees, you will not be able to pass on any of that value to your heirs. If you die earlier than expected, the full purchase of an annuity would mean that much of the fund would be lost.

● SELECTING A PROVIDER

It can be tempting simply to look for the highest rate you can find and take it. However, the long-term security of the annuity provider should be of greater consideration, as should the safeguards you include to protect yourself against inflation. Increasing life expectancy means retirement could now last 20 years or more.

Comparison information on annuities is widely available, so make sure you shop around. We can help you look at the entire market of annuities and select the one that is right for you.

● WHAT TYPE OF ANNUITY SHOULD YOU BUY?

1) Single life or joint life?

This will depend on whether you have a partner for whom you need to provide after your death. If you have a single-life annuity, the income you receive will stop if you die before your partner. If they have no income

provision of their own, this could leave them in a difficult situation that a joint-life annuity would have helped to alleviate. However, as the joint-life annuity will be based on your combined life expectancy, the income you receive from this option will be lower than that of a single-life annuity.

2) Would you like protection against inflation?

Over the long term, inflation erodes the real value of your money. As the cost of living goes up, the purchasing power of your money declines. Even when inflation is running at a low rate, a small fall every year in your disposable income could have a substantial impact over the long term. Protecting your annuity against inflation will cost you more in the short term but may provide peace of mind in the long run.

3) Would you like a guarantee period?

Having saved for years for a decent retirement fund and then purchased an annuity, it is unfortunately possible you might die earlier than expected. This means the annuity will cease and most of the funds accrued over the years will ultimately be wasted. This encourages some retirees to put off buying an annuity for as long as possible. An alternative, however, is to buy an annuity with a guarantee. This ensures a guaranteed income will be paid for the rest of your life or for a specific period. This means, even if you die earlier, your heirs will receive some benefit.

4) Could you accept some investment risk?

Investment-linked annuities invest your money into stocks and shares on the premise that investment growth could increase the potential for higher income payments in the future, without the need for you to buy inflation protection. There are, however, risks to this approach: your investment might not grow, and it might actually fall. Alternatively, even if the investment does grow, it might not grow in line with your expectations. In these circumstances, either your income will have to be cut or it will have to be maintained at the expense of the capital value of your investment. If that possibility troubles you at all, you should stick to conventional annuities.

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5) Do you want to buy from more than one annuity provider?

Although the income from annuities is fixed, retirees still have to take something of a chance on the provider. As the near-collapse of Equitable Life demonstrated, no company is 100% safe. That said, changes in legislation following the problems at Equitable Life mean that annuity providers are now better capitalised, so investors have greater protection than before. However, as with any investment portfolio, you may feel more comfortable spreading your risk across a number of different providers, which could also make other choices easier. For example, you could 'inflation-proof' a part of your income or put a proportion into a joint-life annuity if you need to provide for a dependant.

6) Do you qualify for an 'impaired life' or an 'enhanced' annuity?

If you are suffering from a life-shortening condition, such as heart disease or cancer, you can qualify for an 'impaired life' annuity. Alternatively your lifestyle - for example, if you smoke, are overweight or have worked in a hazardous

occupation - might mean you qualify for an enhanced annuity. Providers work on the basis that certain qualifying medical or lifestyle conditions are likely to reduce life expectancy; therefore an enhanced or impaired life annuity tends to provide a higher annual income on the assumption that it will be paid out for a shorter period.

HAVE YOU CONSIDERED THE 'OPEN MARKET OPTION'?

Over the years, you will have amassed a retirement fund through a company scheme and/or a private plan. Once it's time to begin drawing your retirement benefits, you should inform your pension provider, who will give you a valuation of your pension pot and is also likely to provide you with a quote for an annuity. However, you are under no obligation to purchase an annuity from your pension provider. Your pension provider is legally required to spell out your choices and to ensure you are made aware of the "Open Market Option", which gives you the right to shop around for the best deal for you.