



# Guide to annuities and your options at retirement

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. **Your pension plan provider** will be keen to **give you a quote** for the income that your pension will provide but it would be sensible to take at least a little **time considering** what to do. **Taking the first offer you get** could mean giving up **additional income**.

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

## What is an annuity?



**AN ANNUITY IS A GUARANTEED FIXED INCOME WHICH YOU BUY WITH A LUMP SUM. ITS TERM MAY END EITHER 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 the lump sum which you have built up over the years through a company or private scheme is used to provide you with a lifetime income. However, they can be bought by any investor requiring income, with a cash lump sum from any source.

## What are the retirement rules?



**IT USED TO BE COMPULSORY TO PURCHASE AN ANNUITY AT RETIREMENT. NOW, YOU CAN TAKE A TAX FREE LUMP SUM OF UP TO 25% OF YOUR PENSION FUND AT RETIREMENT AND DEFER YOUR ANNUITY PURCHASE - EVEN AS FAR AS AGE 75 - OR YOU CAN DRAW AN INCOME DIRECT FROM YOUR FUND INSTEAD.**

Alternatively, you can combine annuity purchase, deferral and tax free lump sums so that you retire in stages over several years.

## How is the rate of income determined?



**ANNUITY PROVIDERS HAVE TO DECIDE FOR HOW MANY YEARS THEY WILL HAVE TO PROVIDE AN INCOME.**

Therefore, annuity rates are based on a statistical analysis that calculates how long you are likely to live, given your age, lifestyle and state of health. The rate will also depend on current interest rates.



## 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 (SEE THE ALTERNATIVES OVERLEAF).**

Always remember that you cannot change your choice once it is made so it is important to get that decision right. Annuity rates will change according to the interest rate climate. Therefore, if you are buying at a time in the market cycle when interest rates are particularly low, you may not want to invest your whole retirement fund immediately.

Also, when deciding whether or not to buy an annuity, you should bear in mind that there is no possibility of benefiting from future investment growth on your fund. In addition, unless you have written in certain guarantees, you will not be able to pass your annuity income on to your heirs, so if you die earlier than expected, the full purchase of an annuity will mean that much of that fund will be lost.

## 1 What is the Open Market Option?



**OVER THE YEARS, YOU WILL HAVE AMASSED A RETIREMENT FUND EITHER THROUGH A COMPANY SCHEME OR THROUGH A PRIVATE PLAN. AT RETIREMENT, THE PENSION PROVIDER WILL WRITE TO YOU OFFERING A RANGE OF ANNUITY OPTIONS, ONE OF WHICH WILL BE AN 'OPEN MARKET OPTION'.**

This allows you the chance to take your retirement fund to another annuity provider than the one with whom you have actually built up your fund. It is now a legal requirement to ensure you are made aware of what your open market option will be.



## 2 What type of annuity?



### A) SINGLE LIFE OR JOINT LIFE?

This will depend on whether you have a partner you need to provide for after your death. If you have a single life annuity, the rate of income you get will be based on your age and state of health. If you have a joint life annuity, it will be based on both of your ages and states of health. If your partner is materially younger or healthier than you, you will find that the rate of income is lower. Therefore, you may want to defer your annuity purchase until you can secure a better rate. Women tend to live longer than men and will therefore get lower annuity rates.

### B) DO YOU WANT PROTECTION AGAINST INFLATION?

The inflationary environment has been benign for a number of years. However, earlier this year, inflation figures came in well above the Government's target rate of 2%, demonstrating that the potential for increased inflation still exists. Even with inflation at a relatively low rate, a fall of effectively 2% every year in your disposal income could have an important impact. Protecting your annuity against inflation will cost you more in the short-term, but may give you piece of mind in the long run. Guaranteed pension annuities with fixed increases also offer some protection against inflation.

### C) DO YOU WANT A GUARANTEE PERIOD?

Having saved for years for a decent retirement fund and then bought an annuity, there is the unfortunate possibility that you will die early, the annuity will then end and much of that fund will go to waste. This encourages some retirees to put off buying an annuity for as long as possible. The alternative is to buy an annuity with a guarantee. This guarantees the income will be paid for a set period even if you die, meaning your heirs will reap the benefit.

### D) DO YOU WANT TO BUY FROM MORE THAN ONE PROVIDER?

Although the income from annuities is guaranteed, retirees still have to take a risk on the provider. As the Equitable Life incident 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. As with other types of investment portfolio, retirees may feel more comfortable spreading their risk across a number of different providers, which may make other choices easier. For example, investors can inflation-proof part of their income or put a smaller amount into a joint life annuity to provide for a dependent.

### E) DO YOU QUALIFY FOR AN 'IMPAIRED LIFE' ANNUITY?

If you are suffering from a life-shortening condition, such as heart disease or cancer, you can get an 'enhanced' or 'impaired life' annuity. Some life offices also provide these annuities for 'lifestyle choices' like smoking. In general, the term 'impaired life' annuity is used where there is a reasonable expectation that the person will die within five years. An 'enhanced' annuity is for someone whose life expectancy is reduced.

## Selecting a provider



WE CAN HELP YOU TAKE A LOOK AT THE ENTIRE MARKET OF ANNUITIES AND SELECT THE ONE WHICH IS RIGHT FOR YOU.

It can be tempting to simply look for the highest rate but, as mentioned above, the long-term security of the annuity provider should be of greater consideration. Are they a well-trusted organisation with sufficient capital backing? Do they offer the alternatives you need at a reasonable rate? Comparison information on annuities is widely available, so there are no excuses for not shopping around.



YOU WILL HAVE TO BUY AN ANNUITY ON OR BEFORE AGE 75, BUT UP TO THAT POINT YOU HAVE A NUMBER OF ALTERNATIVE CHOICES.

## What are the alternatives?



### A) DEFERRED ANNUITY PURCHASE

Deferring the purchase of an annuity to older age means the rate is likely to be higher. If you have the flexibility, you may also be able to choose a more favourable time in the interest rate cycle and benefit from any growth in your pension pot for longer. Of course, always be aware that it also means that your retirement fund can be eroded by poor investment performance, lower interest rates or difficult markets, the risk of which must be weighted against the potential gains.

If you defer the purchase of an annuity you can arrange an income draw-down scheme for the interim. Income draw-down means you draw an income direct from your pension funds of up to 120% of the potential annuity income. The rest stays invested until you want to use it to buy an annuity. Investors can vary the amount of income, subject to these Inland Revenue maximum limits. Those who want to continue working could initially draw a smaller pension but increase the amount slowly until retiring fully. Or, take the tax free lump sum but leave taking any income until further down the line.

### B) PHASED ANNUITY PURCHASE

Phased retirement is really a series of mini retirements. It allows you to buy an annuity or draw down income in stages rather than all at once. You decide the level of income you need each year and take that amount from the plan. Clearly, the level of annuity rate will vary as factors like your age and interest rates will change every year.

At retirement, you would get part of your tax-free lump sum, plus a mini-annuity or a mini draw-down plan, which would use up part of your overall fund (up to 25% under current rules). You would then have the option to take more of your tax-free amount and convert more of your pension pot to an annuity or draw-down plan as your needs change. Finally, you convert any remaining part of your retirement fund to an annuity at age 75.

### C) LIFETIME INCOME STREAM

A number of providers are now providing lifetime cash flow products as alternatives to annuities. They will guarantee a certain percentage of invested capital as an income each year for life. Investors retain control of the assets and have access to the remaining capital at any time. These products aim to offer the flexibility of investment bonds with the guaranteed income stream of an annuity and are therefore another important retirement planning option.

## Further information



If you would like to discuss any of the options or issues raised in this guide and how they might apply to you - or if you would simply like information on the best annuity rates available - please do not hesitate to give us a call on the number enclosed.

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