Planning for your retirement

# Your guide to the new world of pensions

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# GREATER FLEXIBILITY, MORE CHOICE IN RETIREMENT

## IN THIS GUIDE



**In his 2014 Budget, the Chancellor announced a series of changes that will have a significant impact on the decisions you face at retirement. These changes will provide you with more flexibility and choice than ever before, putting you in control of your retirement. Put simply, from next April anyone aged 55 or over can take as much of their defined contribution pension savings as they like – when they like. This is good news. It means you and your adviser can design a retirement plan that's right for you and right for your family.**

The introduction of more choice and greater flexibility does mean there are more decisions for you to make. This guide will explain what's happening and describe how different groups of people might respond. This should help you understand the implications of the changes and how they could affect you.

If all this sounds confusing, don't worry, your adviser will help you decide what to do.

### WHAT IS HAPPENING?

The changes fall into two groups:

- Changes that became effective from 27 March 2014.
- Other changes that are planned to take effect from April 2015. (These changes are subject to a government consultation process.)

# CHANGES FROM 27 MARCH 2014

| Drawdown pension | Types of drawdown | Explaining the changes | What are the benefits? | Things to consider |
|---|---|---|---|---|
| Drawdown pension means you can keep your pension savings invested and draw an income which can be varied to suit your needs.<br><br>There are two different types of drawdown pension – capped and flexible. | **Capped drawdown** | Capped drawdown limits the income you can take each year. Broadly, the limit is now increased to 150% (from 120%) of the amount you could receive from a standard annuity. | This change gives capped drawdown clients greater flexibility to take a higher income. | • Taking more income each year is likely to increase your tax bill and could push you into a higher tax bracket.<br><br>• The more income you withdraw each year the greater the possibility that you may run out of money. |
| | **Flexible drawdown** | Flexible drawdown allows you to withdraw as much as you like from your fund, but you have to have a secure pension income in payment of at least £12,000 per year from other sources. Secure income includes State Pensions, defined benefit pensions and annuities. | The reduced minimum of £12,000 means that more people can access their pension fund without restriction. | • The ability to take as much as you like without restriction means the tax you pay could increase.<br><br>• The more you withdraw each year, the sooner your savings will run out. You should ensure you will still have sufficient income to meet your needs. |

| Limited pension savings | Options | Explaining the changes | What are the benefits? | Things to consider |
|---|---|---|---|---|
| If the value of your pension savings is less than a certain amount, you can take these entirely in cash.<br><br>There are two ways you can achieve this. | **Option 1** | If the total value of all your pension pots is less than £30,000 you can take your entire pension savings as a cash sum. | The £30,000 limit means that even if you have a pension fund worth more than £10,000 (see option 2), you can still take this as cash if the total value of all your pension pots is less than £30,000. | • You can still only take 25% of the value of your pension savings as a tax-free lump sum. The balance will be taxable as income in the year you take it.<br><br>• Releasing a lump sum like this could move you into a higher tax bracket and increase your tax bill. |
| | **Option 2** | You can still take as cash any individual pension pots that are less than £10,000. You can take up to three pension pots as cash in this way. | Even if the total value of your pension pots is over the £30,000 limit, if you have small pension pots of less than £10,000 you can take up to three of these as a cash sum. | • You still need an income to live on in retirement and retirement can last a surprisingly long time these days.<br><br>• You need to check with your scheme provider or insurance company to make sure the rules of the pension scheme allow this. |

Please note: In general, 25% of your pension savings can be taken as a tax-free lump sum at retirement. Some older pension arrangements may allow you to take more than this. Your adviser will be able to tell you what you are entitled to.

# CHANGES FROM APRIL 2015

**From April 2015, the government intends to introduce further changes that will have far-reaching effects on how you fund your retirement. The key changes are shown below.**

| What is changing? | What are the implications? |
|---|---|
| There is no longer a requirement to secure an income in retirement. Anyone aged over 55 can take as much as they want at any time from their pension fund. | • You will now have much more choice and flexibility in how you plan your retirement.<br>• The income limits on capped drawdown and the requirement to demonstrate a minimum income for flexible drawdown will no longer apply.<br>• If you are already in drawdown you will still be able to take advantage of these changes.<br>• You will typically only be able to take 25% of your total fund as a tax-free lump sum. The remainder will be taxed as income in the tax year that you take it. This means the more you take, the more tax you may pay. |
| Lump sums payable on death are currently taxed at 55%. The government plans to consult on whether this rate is too high. | • If you would like to leave as much as you can to your dependants, any reduction in tax will be welcome. The current 55% rate has been considered too high by many in the industry. |

Please note that these changes are aimed at people in defined contribution schemes (often called 'money purchase' schemes). If you are a member of a public sector defined benefit scheme ('final salary' scheme), you will not be allowed to transfer your benefits to take advantage of these changes (except in very limited circumstances). The government is consulting on whether it is necessary to introduce similar restrictions for private sector defined benefit schemes. In any event, if you are considering this, we recommend that you speak to your adviser.

It is also worth noting that there will be a consultation process before the changes become effective next April. That means that some aspects of the proposals may be altered. This document is based on our current understanding of what is proposed but we suggest you speak to your adviser before taking any action.

# BE CAREFUL WHAT YOU WISH FOR ...

**Many people will be attracted to the prospect of taking their pension fund savings as cash, but as the case studies that follow will show, there are pitfalls for the unwary. Even if you successfully navigate these, and decide you'd still like to take the cash, think carefully about what you will do with it.**

Most people will need to use some of the money, if not all, to provide an income in retirement. If that sounds like you, how will you decide where to invest?

Leaving it in the bank may be secure, but the returns are likely to be low. Conversely, investing in riskier assets may deliver higher returns, but can also put your capital at risk. You should consider how to manage your pension assets in the context of your other income sources in retirement.

If you'd like help in understanding how to do this, please speak to your adviser.

# RETIRING BEFORE APRIL 2015?

**If you're not sure what to do and you're planning to retire before April 2015, you can still take advantage of the changes.**

The government has announced that you can take your tax-free cash lump sum any time before April 2015, but you won't have to decide what to do with the rest of your pension savings until April 2015 or later (you have 18 months from the date you take your tax-free cash sum to make a decision). You need to check with your provider or insurance company to make sure the rules of the scheme allow this.

To find out more, contact your adviser.

### THE VALUE OF ADVICE

With more choice than any previous generation, a wider range of products available to construct the right solution and significant increases in life expectancy, it's more important than ever to seek professional support and advice. After all, most of us only retire once! That means we have little if any experience of what to do.

# HOW THE CHANGES COULD AFFECT YOU

**To understand how the changes could impact your retirement plans, we've considered a number of different scenarios. Here's a brief description of each followed by a more detailed write-up:**

## CASE STUDY 1: DAVID

"I will be 65 years old this month and want to retire then. I'm entitled to £6,000 a year State Pension and also have a final salary company pension of £10,000 a year that goes up with inflation. I have a personal pension pot of £300,000 and an outstanding mortgage of £50,000. I estimate that I will need just under £18,000 a year before tax to cover my basic living expenses. What can I do?"

## CASE STUDY 2: RICHARD

"I have over £250,000 in my fund, which I'd like to take as cash. I'm happy to take some investment risk. I'm 61 and receive income from a final salary scheme of £15,000 a year."

## CASE STUDY 3: GARETH

"I have £120,000 in my pension plan and I'd like to be able to take this as cash. Can I do this straight away? I'm currently 62 and in receipt of an annual income from a final salary scheme of £10,000."

## CASE STUDY 4: MILLIE

"I'm keen to buy an annuity. I don't want to worry about my money running out, particularly as both my parents are still alive in their 90s. Should I buy now or wait? I'm currently 62 and have £100,000 in my fund after taking tax-free cash. I have no dependants."

## CASE STUDY 5: CHRIS

"I'm keen to leave as much as I can to my dependants when I die. There's a strong likelihood my estate will be in excess of the Inheritance Tax exempt limit. What flexibility do I have to leave as much as possible of my pension fund savings to my estate? My fund is currently worth £400,000 and I'm 66."

## CASE STUDY 6: SHEILA

"I have three pension pots. These are worth £12,000, £10,000 and £8,000. I'd like to take them all as cash. I'm 60 next month. I plan to live on the State Pension and to continue working part-time. My part-time income will be £6,000 a year."

## CASE STUDY 7: PRIYA

"I'm 60 and would like to take my tax-free cash. I have several large credit card debts and a small mortgage – should I take my tax-free cash and repay these? My fund is worth £80,000."

## CASE STUDY 8: JOHN

"I understand that from next year I can take my entire pension as cash. This appeals to me. I'm a 20-a-day smoker with high blood pressure and type 2 diabetes, so who knows how long I will live for? The cash sounds good. I have a fund of £100,000 and I'm 65 years old."

# CASE STUDY 1:
## DAVID WANTS TO BALANCE RISK AND REWARD

"I WILL BE 65 YEARS OLD THIS MONTH AND WANT TO RETIRE THEN. I'M ENTITLED TO £6,000 A YEAR STATE PENSION AND ALSO HAVE A FINAL SALARY COMPANY PENSION OF £10,000 A YEAR THAT GOES UP WITH INFLATION. I HAVE A PERSONAL PENSION POT OF £300,000 AND AN OUTSTANDING MORTGAGE OF £50,000. I ESTIMATE THAT I WILL NEED JUST UNDER £18,000 A YEAR BEFORE TAX TO COVER MY BASIC LIVING EXPENSES. WHAT CAN I DO?"

**First things first – look at clearing debt**
David is entitled to take 25% of his personal pension fund as tax-free cash giving him £75,000 at retirement. In most cases it will make sense to take this cash and as David still has a mortgage of £50,000 he can clear that with part of his tax-free cash. This avoids the need to meet interest and capital repayments out of his taxed income.

**Covering basic expenses – options**
David has a solid base of guaranteed income from the State Pension and his defined benefit plan. Both will go up in line with inflation so he's well protected there. But he hasn't quite got enough to cover his basic expenses. What should he do?

## OPTIONS

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| **Defer State Pension and live off his pension savings for a short period** | For each year that David defers taking his State Pension it will be increased by 10.4%. So by deferring it for three years he will increase it by 31.2% to £7,872 (plus whatever the State Pension has been increased by because of inflation over that period). Together with his defined benefit pension he will then have more or less what he needs to cover his basic expenses and it will be protected from inflation for the rest of his life. He will need to cover excess expenses of £8,000 a year over the three-year period. Assuming inflation is 2% a year this will take around £24,500 from his personal pension savings. |
| **Buy an inflation-proofed annuity of £1,872 a year** | Inflation protection on annuities is an expensive option. The cost of buying an inflation-linked annuity of £1,872 a year (what David would get by deferring State Pension for three years) is just over £54,000.[1] This is over twice what he would need had he chosen State Pension deferral. |
| **Take additional income from his personal pension using pension drawdown** | This is another good option and David certainly has plenty of money to cover this. But it's not guaranteed and so David could find more of his money has to go on covering basic expenses than he intended, particularly if inflation is high. |

Overall, it seems David will be better off deferring his State Pension for three years. He has £25,000 of tax-free cash left after paying off his mortgage and so can use that to bridge the gap for the three years. As he needs certainty of income he holds it on deposit with the bank but can increase his interest by locking it away until he needs it.

## INVESTING FOR INCOME

David has £225,000 left over from his personal pension. What can he do with this?

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| **Use a drawdown pension to stay invested and generate income** | David can invest his remaining fund in a drawdown pension arrangement and access his savings as and when he needs to. Assuming he wants to draw a steady income, then, depending on how certain he wanted to be of his money lasting a lifetime, he could look at a starting income of between 4% and 6% of his portfolio which would generate between £9,000 and £13,500 a year. By investing in growth-oriented assets he could reasonably expect to increase this income over time to help mitigate the impact of inflation. This is not risk-free and if his investments perform poorly he might have to reduce the income he takes or accept the risk of running out of money sooner than expected. |
| **Buy an annuity** | Alternatively David could buy an annuity. With his remaining fund of £225,000 he could buy a flat-rate annuity of around £13,300[2] a year. An inflation-linked annuity would only give him a starting income of £7,600[3] a year. |

As David already has his basic expenses covered he is happy to take some risk in order to grow his retirement income. He invests in a pension drawdown arrangement taking a modest income of £8,000 and investing reasonably adventurously with the aim of growing his income over time and keeping his options open for the future.

[1] Source: Assureweb. Based on a male aged 65 with no health issues and a non-smoker. Annuity purchase price, after tax-free cash has been taken, of £54,036 based on single life, RPI-linked annuity with a ten-year guarantee payable monthly in advance. Figures correct as at July 2014.

[2] Source: Assureweb. Based on a male aged 65 with no health issues and a non-smoker. Annuity purchase price, after tax-free cash has been taken, of £225,000 based on single life, level annuity with a ten-year guarantee payable monthly in advance. Figures correct as at July 2014.

[3] Source: Assureweb. Based on a male aged 65 with no health issues and a non-smoker. Annuity purchase price, after tax-free cash has been taken, of £225,000 based on single life, RPI-linked annuity with a ten-year guarantee payable monthly in advance. Figures correct as at July 2014.

## OTHER CONSIDERATIONS

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| **Benefits on death** | Under a drawdown arrangement any funds remaining on death can be used to provide income for loved ones or withdrawn as a lump sum subject to a tax charge (currently 55%). If David had bought an annuity he could have chosen to have his pension continue to be paid to his wife on death although that would have reduced his income further. |
| **Flexibility** | Annuities once established can generally not be changed. If David's circumstances changed, say his health deteriorated quickly or he needed to fund unexpected expenses, he would almost certainly not be able to change an annuity contract. Drawdown pension would give him the flexibility to change his plans although this might have consequences later on. For example, taking a significant additional withdrawal could reduce the future income he could take. |
| **Management** | A drawdown pension arrangement needs to be reviewed regularly to ensure it remains on track to deliver against expectations. This involves reviewing and adjusting investments and perhaps income levels on a reasonably regular basis. David may be happy doing this himself or may prefer to get the help of a specialist adviser to take care of this for him. In contrast, annuities generally need little maintenance once they are established. |

This example shows that a mix of different income sources is often needed to achieve the best outcome. David used the State Pension, a defined benefit pension and drawdown to get the result he needed. For other people, different solutions might be better. It's important to look at all the options and consider which ones are best for you.

# CASE STUDY 2:
## RICHARD WANTS FULL FLEXIBILITY OVER HOW HE TAKES INCOME

"I HAVE OVER £250,000 IN MY FUND, WHICH I'D LIKE TO TAKE AS CASH. I'M HAPPY TO TAKE SOME INVESTMENT RISK. I'M 61 AND RECEIVE AN INCOME FROM A FINAL SALARY SCHEME OF £15,000 A YEAR."

As Richard has an income of £15,000 from a final salary scheme, he can take his entire pension as cash straight away and doesn't have to wait until the rules change next year. However, unless Richard desperately needs the cash, he should consider the tax consequences of withdrawing such a large sum. He can take 25% of his fund completely tax-free, but the balance would be taxed at his marginal rate. At current tax rates, Richard would pay £77,252 in tax if he withdrew all his money in the same tax year (this includes tax payable on his £15,000 final salary income).

So what are his options?

## OPTIONS

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| **Flexible drawdown** | Richard could withdraw his 25% lump sum immediately and then move the rest into flexible drawdown. This would allow him to manage his income so that he avoids paying higher rate tax. Using this approach, he could take £62,500 as his tax-free lump sum and then a further £26,865 at the 20% tax rate in the first year. With his existing £15,000 income this would take him up to the top of the basic rate tax band and so avoid him paying higher rate tax. In total, this would give Richard £89,365 in the first year. It will take Richard several years to withdraw all his funds using this approach, but he would avoid paying higher rate tax on any of his fund. |
| **Phased withdrawal** | There is an alternative approach where he can achieve the same results, but with significant tax advantages. This involves phasing withdrawals over a number of years. This approach would take longer to withdraw the money than the previous option, but there are tax advantages on his death should Richard die before all the money is withdrawn. |

Richard should bear in mind that he will still require an income to live on throughout his retirement. Consequently, he should consider staying in pension drawdown or perhaps using part of his fund to buy an annuity.

Remember if you're in a similar position to Richard, your adviser will be familiar with these issues and is well-placed to offer the help and support you need to reach the right decision.

# CASE STUDY 3:
## CAN GARETH TAKE HIS £120,000 PENSION AS CASH?

"I HAVE £120,000 IN MY PENSION PLAN AND I'D LIKE TO BE ABLE TO TAKE THIS AS CASH. CAN I DO THIS STRAIGHT AWAY? I'M CURRENTLY 62 AND IN RECEIPT OF AN ANNUAL INCOME FROM A FINAL SALARY SCHEME OF £10,000."

There is a way that Gareth can access his pension savings and take everything as cash. It's called 'flexible drawdown' and it allows Gareth to take as much as he wants from his pension fund at any time.

However, to take advantage of flexible drawdown there are two criteria Gareth must meet:

- He must be in receipt of a minimum income of at least £12,000 a year
- The income must meet the qualifying conditions. For example, State Pensions or a final salary pension are acceptable, but not all income qualifies

Gareth only has qualifying income of £10,000 from a final salary scheme. What are his options?

[1] Source: Assureweb. Based on a male aged 62 with no health issues and a non-smoker. Annuity purchase price, after tax-free cash has been taken of £36,000, based on a single-life, level annuity with a ten-year guarantee payable monthly in advance. Figures correct as at July 2014.

## OPTIONS

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| **Wait until April 2015** | From April 2015 the Minimum Income Requirement no longer applies. He could simply wait until then. |
| **Meet the Minimum Income Requirement** | Gareth could use some of the money in his pension fund to buy an annuity that would provide an annual income of £2,000. This would cost around £36,000[1] leaving him £84,000 that he can then draw out through flexible drawdown. This would reduce the overall amount he can access as cash, but he would meet the £12,000 Minimum Income Requirement. |
| **Access his tax-free cash and take income** | There are options that would allow Gareth to take his tax-free cash now plus take an income for the next 12 months. Gareth could then release the rest of his fund next April. Note that this would mean that if Gareth died before withdrawing the balance of his fund the remainder would be taxable at 55% (though this rate is being reviewed). |

However, while this may be what Gareth would like to do, does this approach make sense? Here are a few considerations that he and his adviser should think about.

## THINGS TO CONSIDER

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| **Tax position** | Only 25% of the fund can be taken tax-free, with the balance taxed as income. Given the significant sums involved, a sizeable amount of the money would be taxed at higher rates. Gareth would do well to consider phasing the withdrawal of his funds to reduce the amount of income tax he will pay. |
| **Income in retirement** | Retirement can last 20–30 years these days. That means Gareth should think about investing at least some of the money to provide an income in retirement to supplement his final salary pension. For example, he could buy an annuity or remain in drawdown and take an income from the fund. |

# CASE STUDY 4:
## MILLIE'S UNCERTAIN WHETHER TO BUY AN ANNUITY NOW OR WAIT

"I'M KEEN TO BUY AN ANNUITY. I DON'T WANT TO WORRY ABOUT MY MONEY RUNNING OUT, PARTICULARLY AS BOTH MY PARENTS ARE STILL ALIVE IN THEIR 90s. SHOULD I BUY NOW OR WAIT? I'M CURRENTLY 62 AND HAVE £100,000 IN MY FUND AFTER TAKING TAX-FREE CASH. I HAVE NO DEPENDANTS."

There's much discussion around the value of annuities. Most of it centres on average life expectancy. For example, women aged 65 have an average life expectancy of almost 86 years of age. However, averages are deceptive. Around 50% of people will die before 90 and 50% will live longer. Millie's parents are still alive in their 90s and there are now over 13,000 centenarians in the UK.

Faced with the prospect of living to a ripe old age, Millie is right to seriously consider an annuity. However, the question of whether to buy now or wait is more difficult. Here's an analysis of the options.

## OPTIONS

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| **Buy an annuity now** | Buying an annuity now will provide peace of mind. Millie will know that she has secured a guaranteed income for life and can get on and enjoy her retirement. She'll also qualify for State Pensions when she reaches State Pension Age, as well as a host of other benefits like a free bus pass and Winter Fuel Allowance. She will also no longer pay National Insurance contributions. So if she can live on the income she could generate, she should think about buying an annuity now. |
| **Wait and buy an annuity at a later date** | The benefit of waiting is that annuity rates may improve. This means Millie could have more money during her retirement. It is perfectly possible that annuity rates may rise over time, but equally they could remain where they are or reduce even further. |
| **Phase the purchase of an annuity** | Millie could phase the purchase of an annuity. For example, she could buy an annuity costing £20,000 each year for the next five years. In this way, if annuity rates did improve she would benefit in part, and if annuity rates should worsen over time she would have secured part of her income at the earlier higher rates. Some companies offer better rates for higher premiums and Millie should check that she would not lose out by buying in phases. |

Millie would do well to discuss these options with her adviser to make sure she fully understands the pros and cons of each approach before making a decision.

# CASE STUDY 5:
## CHRIS IS KEEN TO LEAVE AS MUCH TO HIS FAMILY AS HE CAN

"I'M KEEN TO LEAVE AS MUCH AS I CAN TO MY DEPENDANTS WHEN I DIE. THERE'S A STRONG LIKELIHOOD MY ESTATE WILL BE IN EXCESS OF THE INHERITANCE TAX EXEMPT LIMIT. WHAT FLEXIBILITY DO I HAVE TO LEAVE AS MUCH AS POSSIBLE OF MY PENSION FUND SAVINGS TO MY ESTATE? MY FUND IS CURRENTLY WORTH £400,000 AND I'M 66."

Chris wants to maximise his estate after he dies. Different solutions attract different rates of tax on death so it is worth thinking about this issue at the time of selecting a retirement solution. Here's an overview of the tax efficiency of different products on death.

## OPTIONS

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| **Phased withdrawal** | Phased withdrawal can be a very effective method for someone like Chris who wants to leave as much as possible after his death. If you would like to find out more about how this works please speak to your adviser. |
| **Drawdown pension** | Drawdown pension means Chris could keep his pension savings invested and draw an income which can be varied to suit his needs. At the moment, there are limits on how much you can take, but these limits will no longer apply after April 2015.<br><br>On death, Chris's partner or family can continue to carry on withdrawing an income and these payments will be subject to income tax.<br><br>Alternatively, whatever remains in the fund can be distributed, but if Chris has accessed his savings through drawdown there is a tax charge of 55% on any lump sum payable on death. The government is reviewing the 55% tax charge and this may be reduced in the future. |

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| **Annuities** | If Chris is planning to leave as much as he can to his family, annuities aren't necessarily the best solution in that there is often no further payment on death. However, there are exceptions to this general comment:<br><br>• Guaranteed periods. Chris can choose an option that allows for his income to continue to be paid for a fixed period after his death. Commonly, people select either five to ten years. This means if Chris chose a ten-year guaranteed period, and died three years after buying the annuity, the remaining seven years' payments would continue to be made. The payments will be subject to income tax. In some circumstances, the payments may be made to his estate and could be liable for Inheritance Tax.<br><br>• Value protection. This option means that whenever Chris dies his estate will receive all of his original investment, less the payments made up to the date of his death. Be aware that the payment will be subject to a 55% tax charge (though this is being reviewed by the government and may reduced in the future).<br><br>With an annuity Chris can also choose a spouse's pension so that his spouse or partner continues to receive an income for the rest of their life after his death. |
| **Take pension fund as cash** | From April next year Chris could take his entire pension as cash. However, it will be taxed at his marginal rate which would be 45% on most of the fund (though he could withdraw funds over many years to avoid paying higher rates of tax). If he invests the money it will form part of his estate on his death and will be subject to 40% Inheritance Tax if he's in excess of the exempt limits (these are currently £325,000 for a single person or £650,000 for a couple). However, he could make what are known as 'potentially exempt transfers' during his life. This means any gifts Chris makes during his lifetime will not be liable for Inheritance Tax if he survives for seven years after making the gift. There is no limit on the amount that can be transferred in this way. |

# CASE STUDY 6:
## SHEILA WANTS TO CASH IN HER SMALL PENSION POTS

"I HAVE THREE PENSION POTS. THESE ARE WORTH £12,000, £10,000 AND £8,000. I'D LIKE TO TAKE THEM ALL AS CASH. I'M 60 NEXT MONTH. I PLAN TO LIVE ON THE STATE PENSION AND TO CONTINUE WORKING PART-TIME. MY PART-TIME INCOME WILL BE £6,000 A YEAR."

The good news is Sheila should be able to cash in all her pension pots without having to wait until the more far-reaching changes take effect next year. The Chancellor announced an increase in the amount that can be taken in cash, effective from 27 March this year, to £30,000 and in addition, up to three pension pots of up to £10,000 can be taken in cash even if the £30,000 limit has been breached. However, there are a few considerations that Sheila should bear in mind.

## OPTIONS

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| **You have to be 60 or over** | Luckily, Sheila is 60 next month. Generally, benefits can be taken from age 55, but the age limit if you want to take limited pension savings entirely as cash is 60. |
| **The scheme rules must allow this to happen** | Although the Chancellor announced this change with effect from 27 March, schemes don't have to allow it. Sheila should check this first. |
| **There are no other pension savings** | If Sheila had other pension savings these would push the total value over £30,000. This would mean she could not take all her pension pots as cash now, but she could still take the two pension pots that are less than £10,000 as cash and then cash in the larger pot next April. |

On the assumption that Sheila's scheme has changed its rules and that she has no other pension savings, she can take all her pension pots entirely as cash once she turns 60. However, before she finally chooses this route there are other aspects to consider:

## THINGS TO CONSIDER

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| **Only 25% of the total cash is tax-free** | Although all the pots can be taken as cash, only 25% of the amount is tax-free. Sheila's part-time earnings take her up to the amount she can earn without paying tax. That means she'll pay 20% tax on the rest of her pension fund (after the tax-free cash has been taken). This amounts to a tax bill of £4,500. |
| **It could affect entitlement to long-term care and other means-tested benefits** | Whether you have to pay for means-tested benefits like long-term care depends on your total assets. Proposals for paying for long-term care scheduled to take effect from 2016 exclude pensions, but having opted for cash it is likely to be taken into account (if it hasn't been spent). |
| **You still have to live in retirement** | Retirement can last 20–30 years these days. That means Sheila should consider using at least some of the money to boost her income. She plans to continue working part-time and live off these earnings plus the State Pension. However, her State Pension won't be payable until she's 65 and she may not be able to work indefinitely. |

# CASE STUDY 7:
## SHOULD PRIYA TAKE HER TAX-FREE CASH AND REPAY HER DEBTS?

"I'M 60 AND WOULD LIKE TO TAKE MY TAX-FREE CASH. I HAVE SEVERAL LARGE CREDIT CARD DEBTS AND A SMALL MORTGAGE – SHOULD I TAKE MY TAX-FREE CASH AND REPAY THESE? MY FUND IS WORTH £80,000."

It usually makes sense to pay off debt where possible and the tax-free cash sum is a good way to achieve this. The interest Priya pays on her credit card debts is likely to be higher than the return she could achieve by investing the money – unless she's prepared to invest in riskier investments that may fall in value as well as rise. Priya's fund of £80,000 means she can take £20,000 completely tax-free.

## THINGS TO CONSIDER

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| **Early repayment penalties** | If there are any early repayment penalties these should be considered carefully when weighing up when to repay debts. In some cases, early repayment can trigger an additional penalty that may make it worthwhile maintaining the debt (at least until any penalties no longer apply). These are not normally applicable to credit card debt, but Priya should check. |
| **Competitive fixed rates** | If Priya has the benefit of a great fixed rate deal she might earn more with her money if she invested it. Again, this assumes she doesn't have to take significant risks with the money she invests. |
| **Prioritising debts** | If Priya can't pay off all her debts by the time she retires, she should consider paying off the debts which are costing the most. Not in terms of her monthly repayments necessarily, but the interest rate paid. Generally, short-term debt, like credit cards, will attract higher interest rates than long-term debt, like mortgages. |

However there are a few things to bear in mind before Priya repays her debts. She will also need to consider what to do with the rest of her pension fund and she has 18 months to decide. This will take her beyond April 2015 when the government changes take effect so she will have more choice and flexibility. She should also bear in mind that, having taken the tax-free cash, on her death, tax will be payable on her remaining pension fund savings at 55% (though this rate is being reviewed and may reduce). Priya's adviser will ensure she makes the right decision by taking into account all these considerations.

# CASE STUDY 8:
## JOHN IS A SMOKER WITH DIABETES AND HIGH BLOOD PRESSURE

"I UNDERSTAND THAT FROM NEXT YEAR I CAN TAKE MY ENTIRE PENSION AS CASH. THIS APPEALS TO ME. I'M A 20-A-DAY SMOKER WITH HIGH BLOOD PRESSURE AND TYPE 2 DIABETES, SO WHO KNOWS HOW LONG I WILL LIVE FOR? THE CASH SOUNDS GOOD. I HAVE A FUND OF £100,000 AND I'M 65 YEARS OLD."

John assumes that because he's a smoker with diabetes and high blood pressure he isn't likely to enjoy a long life. Certainly, there is overwhelming evidence that, on average, smokers like John with high blood pressure and diabetes aren't likely to live as long as healthy, non-smokers. However, though John may die earlier than his average life expectancy, he can't be certain. So what are his options?

## OPTIONS

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| **Take the cash and spend it while he's still able to enjoy it!** | John may not plan on a long retirement, but what if he's wrong? Even if he dies earlier than the average life expectancy for a 65-year-old, how much earlier? This uncertainty makes it difficult for John to assess how much income he should take each year. He'll also pay tax if he takes all his pension fund savings at once. |
| **Drawdown pension** | From April next year, John could take as much or as little from his pension fund as he chooses using a drawdown pension (this is also an option at the moment if John can demonstrate he is in receipt of an income of £12,000 a year or more). He could also withdraw all his pension fund monies if his health was deteriorating rapidly. |
| **Buy a bespoke annuity based on his medical conditions (enhanced annuity)** | An enhanced life annuity takes account of any medical conditions that could shorten life expectancy. John's health and lifestyle could mean he's offered substantially more than the income offered to a healthy person of the same age, irrespective of how long he lives. For example, at current rates, John could be offered £5,302[1] (this figure may vary based on the seriousness of his medical conditions). This compares with an annuity for a healthy, non-smoker, 65-year-old of £4,522.49.[2] |

## THINGS TO CONSIDER

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| **Tax position** | If John takes all his pension savings as cash he will pay tax at his highest rate. If his fund is worth £100,000 he can take £25,000 tax-free, but £75,000 would be taxed. If John has no other income, he would pay tax of £19,627. Income from an annuity or drawdown pension is taxed, but John should be able to manage his income so that he only pays standard rate tax. |
| **Death benefits** | It sounds as though John isn't concerned about leaving money after his death, but it is worth bearing in mind that the treatment of the three options on death varies significantly. |

These are just some of the questions that John should speak to his adviser about.

[1] Source: Assureweb. Based on a male aged 65 with high blood pressure taking one prescribed medication for the condition and type 2 diabetes taking one prescribed medication for the condition plus smoking 20 cigarettes each day. Annuity purchase price, after tax-free cash has been taken, of £75,000 based on single life, level annuity with a ten-year guarantee payable monthly in advance. Figures correct as at July 2014.

[2] Source: Assureweb. Based on a male aged 65 with no health issues and a non-smoker. Annuity purchase price, after tax-free cash has been taken, of £75,000 based on single life, level annuity with a 10-year guarantee payable monthly in advance. Figures correct as at July 2014.

# THE IMPORTANCE OF ADVICE IN MAKING THE RIGHT DECISIONS

**The changes to pensions will significantly impact how people organise their finances at retirement.**

With greater choice than any previous generation, a wider range of products available to construct the right solution and significant increases in life expectancy, it's more important than ever to seek professional support and advice. After all, most of us only retire once! That means we have little if any experience of what to do.

The wrong decisions can be costly. What's more, some of the decisions you take now may be irreversible.

Your retirement savings have to provide an income each year for the rest of your life (and these days retirement can last an awfully long time). Take the time to make the right decisions for you and your family.

**IMPORTANT INFORMATION**

The value of investments can go down as well as up and you may get back less than you invest. Past performance is not a guide to what may happen in the future.

Tax savings and eligibility to invest in a pension or an ISA depend on personal circumstances and all tax rules may change in the future. Please note, you cannot access the money held in a pension until the age of 55.

If you are using pension drawdown, you and your adviser control, and must review how your pension is invested, taking into account your attitude to risk, and the level of income you take. Market volatility or high income withdrawals, may result in your pension pot reducing in value, leaving you with less income than you need in future.

The information contained in this guide must not be deemed as advice, and any advice you do receive must be provided by your adviser.

## Contact your adviser to help you get in shape financially for retirement.