

The Annuity Direct Guide to Unsecured Pensions



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The
Retirement
Income
Specialists

An *Annuity Direct* guide to help you understand your retirement income planning

The Annuity Direct Guide to **Unsecured Pensions**

This guide has been prepared to help you understand unsecured pensions. It provides an introduction to unsecured pensions, looks at some of the benefits and risks of an unsecured pension and then takes you through the issues you may encounter and the decisions you may have to make when thinking about using an unsecured pension as a way of providing income for your retirement.

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Please remember the information contained in this leaflet is only a guide and to help you understand the issues relevant to you, your Retirement Income Specialist is always available to advise you or talk about any concerns you may have. Do not hesitate to email them, or give them a call.

So What Is An Unsecured Pension?

An unsecured pension (sometimes called Income Drawdown, or Pension Fund Withdrawal) enables you to do four things at the same time:

1. Take any tax-free cash you're allowed from your pension scheme.
2. Withdraw money from your pension fund to use as an income until you're ready to buy an annuity (or draw your pension)
3. Leave your pension fund to grow in a tax-efficient investment environment, and pay in contributions if your original scheme rules allow.
4. Vary your income each year (within pre-defined limits) dependent upon your need.

How is an Unsecured Pension Different From an Annuity?

An unsecured pension works quite differently from a pension annuity and is considered the highest risk of all the investment-linked retirement income products.

It is designed for people with larger pension funds, say £200,000 or more, or who have considerable other assets and the minimum fund any provider will agree to accept is normally £100,000. You can put your whole fund into drawdown or just some of it. There are rules governing what income you can take.

If you are considering an unsecured pension as a way of providing income for your retirement, please read the rest of the booklet, but more importantly, speak to your Retirement Income Specialist who will be able to help you understand the investment risk as well as the potential benefits of unsecured pensions.

So What Are the Benefits of an Unsecured Pension?

If you are currently unsure of your medium to long-term retirement plans, but need some income and/or tax-free cash, you might want to consider an unsecured pension.

Outlined are some of the potential benefits of unsecured pensions, along with the associated risks.

Income Flexibility

If you don't have a steady income because your earnings are variable or seasonal, an unsecured pension lets you top them up on a regular or occasional basis by taking any amount within an upper and lower limit each year, letting you choose when and how to take your income,

eg - regular and/or one-off amounts when you need the money.

You can also continue paying into any part of your pension that's not included in the unsecured pension, if you wish.

The risks - on the downside, when you finally convert what's left of your pension fund to an annuity, it's

possible to end up on a smaller lifetime income than if you'd converted to an annuity in the beginning.

This could happen if investment returns have been poor, you've been taking the maximum income from your unsecured pension, or annuity rates have fallen.

You should also be aware that you will not receive any cross subsidy from the funds of those who die early, as is the case with an annuity. This is termed mortality drag. This means that the unsecured pension fund must achieve an additional growth each year to replace this loss.

Current Poor Health

People with a potentially life threatening illness, rapidly deteriorating condition or a terminal illness often want to pass on their pension fund to their next of kin when they die, instead of tying it up in an annuity.

An unsecured pension allows this to happen (although the lump sum paid out on death is taxed).

The risks - depending on your condition you may qualify for an 'enhanced rate annuity'. This would pay you a higher than normal income

If you use an unsecured pension, and you survive more than 5 years, you might not qualify for an enhanced rate annuity later on. So, when you finally buy an annuity, you'll be much worse off.

Expected Poor Health in the Future

People with a history of family illness may be concerned that it could happen to them too. For this reason they may decide to delay buying an annuity thinking that if they do become ill, they'll get an enhanced rate. This may be true – but conversely 'it' may never happen.

The risks - if you remain healthy and delay buying an annuity for more than a year, you could easily be worse off especially if investment performance is poor or annuity rates drop in the meanwhile. If you do become ill, the condition itself may not be serious enough to warrant an enhanced rate, or the enhancement may not outweigh the income sacrificed in the interim.

What Protection is There Against The Risks?

Your pension fund must last your whole retirement, therefore pension rules require you to buy an annuity before you reach age 75. The only alternative is to move to an *Alternatively Secured Pension (ASP)* which allows you to continue to draw from the fund, beyond the age of 75.

In this case death benefit is taxed at a penal rate, unless the fund is left to a charity. The amount of income you may take is based on the annuity a 75 year old person could obtain.

To ensure you have sufficient funds to invest in an annuity or ASP at age 75, an unsecured pension should have some built-in safeguards to help stop the fund dwindling if investment performance is not enough to support the amount you withdraw.

Income Limits

The Government puts restrictions on how much you can withdraw. The lower limit is zero, rising to a maximum based on your age, size of fund and current economic conditions. Within these limits, you

Protection Against the Risks

choose how much to take out each year, the type of payments and when to take them. This could be;

- one or more lump sums.
- regular monthly, quarterly, half-yearly payments or annual.
- a combination of lump sums and regular payments.

You must take no more than the maximum.

5 yearly Income Reviews

To try and ensure you don't deplete your pension fund, your income limits will be reviewed every 5 years. The new ones will be based on:

- your age at the time.
- the amount of pension fund you have left.
- current economic trends, especially gilt yields.

After each review, the new income limits could be higher or lower than the old ones.

Extra Flexibility

You have considerable freedom, especially when compared to an annuity. For example you can:

- move to another unsecured pension provider at any time
- switch into any type of annuity,

with any provider at any time up to age 75

- alter the amounts of income you take and when you take it – within the allowed limits
- change your investment approach depending on market conditions, or other reasons.

In addition in the event of your death, the fund is returned subject to taxation at 35%(rate at date of publication)

Unsecured Pensions can be an attractive solution to the client who has sufficient wealth to withstand a fall in income. It should not be entered into lightly and your Retirement Income Specialist will help you understand the risks associated with this and how they interact. We will only recommend this approach to clients who have understood and are comfortable with the risks involved

If you are comfortable with the risk that your income may fall in order to benefit from investment performance, ask your Retirement Income Specialist, to calculate the annual yield that would be needed on your fund, to enable you to enjoy a continuing income at the level that an annuity might provide today.

Making the Next Move

The next thing you should do, is to contact your Retirement Income Specialist for more information or advice, and to help you begin to plan your retirement income. You can phone or email them direct.

Alternatively you can speak to any other member of the Annuity Direct Income Specialist team on **0500 50 65 75**

We also have a comprehensive website with more information about Annuity Direct, the services and products we advise on , as well as other helpful links. **www.annuitydirect.co.uk**

There are also a range of other guides and information leaflets which you can request for *your retirement income specialist* to send to you. These include:

- *The Annuity Direct Guide to Pensions*
- *The Annuity Direct Guide to Guaranteed Annuities*
- *The Annuity Direct Guide to Purchased Life Annuities.*
- *The Annuity Direct Guide to Equity Release*
- *The Annuity Direct Guide to Retirement Income and Taxation*
- *The Annuity Direct Guide to Planning Retirement Income*



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