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Community Hub

Your Retirement Options Explained

Taking care of your tomorrow.

Davidson Asset Management Ltd

Quick Guide:

	Annuity	Flexible Access (Flexi-Access Drawdown)	Lump sum
How will I access the money?	An annuity provides a regular and secure income for life (or the term of the annuity if this is for a set period).	You can chose to access tax-free cash and/or income from the pension (subject to income tax) at any time. This can be set up on a monthly/ quarterly/ ad-hoc basis and any funds untouched can remain invested.	A lump sum is paid (up to the max full value of the plan). No regular income.
How does tax free cash work?	Tax-free cash can be provided at outset before purchasing your guaranteed income.	25% tax-free cash can be accessed at any time (either as an initial lump sum or as required).	Immediate access to as much of the fund as required. Of the amount paid out, 25% is paid free of tax with the rest subject to income tax.
How does the income pay out?	Your annuity income is paid at least annually and can increase, decrease or remain level in payment, either for the rest of your life or term of the annuity.	You can choose the income you want, and when you want it. This can be monthly or ad-hoc.	You can choose when and how much of a lump sum you require.
What are the death benefits?	Additional options can be selected at outset such as spouse's pension or guarantees after death that the income will continue for a set period of time.	On death, if there is any fund remaining then it is available to be passed on to your beneficiaries.	On death, if there is any fund remaining then it is available to be passed on to your beneficiaries.
Are there any implications once I have accessed the pension?	Once you have bought your annuity, you usually cannot change your mind or change benefits.	Once you have accessed 'taxable' income from the pension, this will trigger the money purchase annual allowance, (which limits how much yourself/employer can pay into the pension going forward).	Once you have accessed 'taxable' income from the pension, this will trigger the money purchase annual allowance, (which limits how much yourself/employer can pay into the pension going forward).

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Annuity:

Overview

An annuity is simply a series of payments made at selected intervals normally on a monthly basis. The level of payment is dependent upon age, annuity rate, size of fund and options selected. Annuity rates tend to mirror interest rates, therefore when interest rates are higher, annuity rates tend to be better, meaning you would get a higher income in return. There are many different types of annuities and these are covered later on in this section.

Tax Free Cash

Most types of pension plan have the option of taking a tax-free cash lump sum before exchanging the residual fund for an annuity. Once an annuity has been purchased there is no further entitlement to tax-free cash, therefore the decision of whether to access the cash or not needs to be made at outset.

Income

Annuity payments are taxed at source under the PAYE system. Payments can be made monthly, quarterly, half yearly or yearly and can be in advance or arrears. Payments can remain level, can decrease or can increase e.g. at a set rate or in line with an index such as the Retail Prices Index.

Death Benefits

The option of what type of death benefits to include must be made at outset. The options available are as follows:

- A spouse's or dependents pension up to 100% of the pension you had received.
- A lump sum.
- A guarantee that your pension will pay out for a set period of time, for example 20 years . This means that if you were to die in year 15, the annuity would pay out for a further 5 years. If you died in year 21, the annuity wouldn't pay out on death as the guarantee period has passed.

Advantages

- You will receive a guaranteed income for life, and you can elect for your spouse/beneficiaries to receive a guaranteed income or a lump sum upon your death.
- Tax-free cash is available at outset.
- There are no additional charges applied to the contract once in force. All charges are taken at outset and are reflected in the annuity rate offered.
- The contract is simple to understand, there is no need to review the contract and there is minimal paperwork needed to start the payment of benefits.

Disadvantages

- There is no opportunity of participating in future investment returns.
- The various options in relation to death benefits and increasing / decreasing income levels etc must be selected at outset.
- Once the income has commenced, this cannot be altered offering minimal flexibility.

Suitability

Lifetime annuities are most likely to suit individuals who want an absolute guarantee on their pension payments and/or for their spouse/partner. They suit individuals with low risk appetite and a requirement for security. They also suit individuals who have relatively small pension funds and who will be heavily reliant on their pension income.

Flexible access:

Overview

With Flexi-Access Drawdown (FAD) - you can choose to take as much or as little of your pension as you wish and it will be added to any other income to determine the tax rate that will apply. Please note that if you draw any income from this plan, any future pension contributions will be capped due to the money purchase annual allowance. This is set at £10k per annum (2025/26 tax year).

Income

A pension income does not have to be taken from the pension (if you only require tax-free cash) but if this is required, income is taxed as earned income under the PAYE system.

Death Benefits

On death before age 75, the funds remaining in the plan will be paid out tax-free whether they are paid as a cash lump sum or in pension format. On death after age 75, the same options apply. However, tax will be payable at the beneficiaries marginal rate of income tax.

Advantages

- You are able to take all of your tax-free cash lump sum entitlement at outset.
- You do not receive a set income but are able to vary it to suit your personal circumstances, to supplement other sources of income.
- The flexibility can offer the ability to more carefully manage your liability to personal income tax in certain years.
- You have the potential to benefit from good investment performance in a tax-efficient environment and to exercise control over your own investment portfolio.
- There are flexible death benefits.

Disadvantages

- You may run out of money and have no pension left. High income withdrawals may not be sustainable during the deferral period.
- Benefits are means tested by the DWP.
- Taking large withdrawals may erode the capital value of the fund, especially if investment returns are poor and a high level of income is being taken. This could result in a lower income when the annuity is eventually purchased and could also affect the long term financial security of your spouse/partner.
- A careful investment portfolio needs to be constructed which will involve some investment risk. This means the fund value could fall which could affect your future income levels.
- Increased flexibility brings increased costs and the need to review arrangements on an on-going basis.

Lump Sum:

Overview

With this option, you can withdraw as little or as much as you wish from your plan and any payment will allow for 25% of the monies to be paid tax free and the remainder will be subject to your marginal rate of income tax. Please note that if you draw any income from this plan, any future pension contributions will be capped due to the money purchase annual allowance. This is set at £10k per annum (2025/26 tax year).

Death Benefits

On death before age 75, the funds remaining in the plan will be paid out tax-free whether they are paid as a cash lump sum or in pension format. On death after age 75, the same options apply. However, tax will be payable at the beneficiaries marginal rate of income tax.

Advantages

- You are able to take as much or as little of your existing pension plan as necessary.
- It offers one of the most straightforward and simple options for pension payments at retirement.

Disadvantages

- You may run out of money and have no pension left
- Benefits are means tested by the DWP.
- Any funds remaining in the plan are subject to investment risk. This means the fund value could fall which could affect your future income levels.
- You may feel that the flexibility of having payments made in the form of a lump sum as and when required does not compensate for the known income available from an annuity now and for the rest of your life.

If you would like further information on the topics covered within this document, please speak to your DAM Advisor

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