

Buying an annuity

Will you get the maximum retirement income when you retire?

Whether your retirement is a long way off or just around the corner, it's important to think about how much income you're likely to have. And as you approach retirement, you'll also have to decide how you'd like to receive the money from any pensions you've been saving towards. The most popular way of securing an income for life is by converting your pension fund into an annuity.

A guaranteed income for life

An annuity provides you with a guaranteed income for life when you retire. You buy an annuity using a lump sum from your pension or, perhaps, some savings. Annuities remove the worry of having to budget for an unknown period of time.

You can buy your annuity from any provider and it certainly doesn't have to be with the company you had your pension plan with. The amount of income you will receive from your annuity will vary between different insurance companies, so it's essential to shop around for comparisons before making your decision. This could be an expensive mistake if you get it wrong. The difference between the annuity rates will be dependent on the annuity terms selected.

Annuities can't be changed once set up so it is vital you secure the best possible income. Even though you don't have to stay with the company your pension is currently held with, many people still do.

Types of annuity

Pension Annuity

A Pension Annuity is bought using money from your pension fund. It may be appropriate if you require a guaranteed income for life, based on the value of your pension, and want to choose whether your income stays the same or increases each year. You could also qualify for a higher income due to a previous or existing medical condition your partner or you have or had.

An annuity promises to pay you a guaranteed regular income for life. You have the choice to receive your annuity income monthly, quarterly, half-yearly or annually. Payments can be 'in advance' (from the start date) or 'in arrears' (at your chosen payment interval after the start date).

If you don't have a clean bill of health or you have (or have previously had) one of a range of medical conditions affecting your health or longevity, you may receive a higher income. You may also be eligible due to certain lifestyle conditions, such as if you smoke or are overweight.

Once started, this type of annuity income will not usually go down, even if your health, or your spouse's health if applicable, improves. Depending on how long you live, you may get back less than you bought your annuity for. Once you've bought an annuity it cannot be cashed in at any time and there is no cash-in value.

You can take out an annuity that stops whenever you die. Or, alternatively, you can choose an annuity with a smaller income, but which is guaranteed to be paid for a period between one and ten years. This is called the 'guarantee period'. The options you choose at the start of your plan can't be changed.

With-Profits/Investment-linked Pension Annuity

If you'd like to give your retirement income the potential to grow and you're happy to accept an element of risk, you could choose this annuity that invests in a with-profits or unit-linked fund. With this option, the amount of income you receive has the potential to increase over time.

It guarantees to pay an income to you for the rest of your life. The underlying annuity fund is invested in a wide range of investment assets and the income payable to you each year depends on the investment returns of those assets and in the case of a with profits annuity, the initial bonus rate selected.

This is a stock market related investment. Your income can vary from year to year and could go down. However, your income will never fall below a certain guaranteed level in the case of a with-profits pension annuity.

Your income can be paid monthly or yearly, either 'in advance' (from the start date) or 'in arrears' (at your chosen payment interval after the start date). The amount of income you receive has the potential to go down as well as up.

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A pension is a long-term investment. The fund value may fluctuate and can go down as well as up. You may not get back your original investment. Past performance is not an indication of future performance. Tax benefits may vary as a result of statutory change and their value will depend on individual circumstances. This is for your general information and use only and is not intended to address your particular requirements. It should not be relied upon in its entirety and shall not be deemed to be, or constitute, advice. Although endeavours have been made to provide accurate and timely information, Goldmine Media cannot guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No individual or company should act upon such information without receiving appropriate professional advice after a thorough examination of their particular situation. We cannot accept responsibility for any loss as a result of acts or omissions taken in respect of any articles. Thresholds, percentage rates and tax legislation may change in subsequent Finance Acts.