Retirement Planning

(Personal Pension Plans)

A Summary Guide

01903 244980

advice@affinityfinance.net

www.affinityfinance.net

General Overview

We all have a need to plan for our retirement, and we should take responsibility to ensure this happens with an acceptable predicted outcome.

During the 18th Century the poor relied on the **Elizabethan "Poor Laws"** whereby the parishes had to support the poor and sick but not the "work shy". Thanks to the efforts of a few champions of the common folk, such as Charles Dickens, by the end of the 19th century, state intervention took the leading role in providing for the elderly.

In 1908 Prime Minister Lloyd George introduced a means tested flat rate five shillings a week, paid to the poor aged seventy plus. A few years later in 1925 the statutory **State Pension** was introduced for all men from the age of 65.

At this time the average male life expectancy was less than 70; and the State Social Security System had very few other financial obligations to meet. The average male life expectancy is now 84 and rising; and today's Department of Work & Pensions has to provide for both men and women, together with many other employment based obligations.

This places the **State Pension** under a considerable and ever increasing strain to keep up with the needs of the nation. Although it is still a reliable starting point, it may not always be there as we know it today, or be enough to provide the required standard of living. Therefore, if you want to command your own retirement income you need to do something else about it.

But why would anyone want to be a part of Pension Savings after so many scandals and failures? Well, the answer is that not all Pension Plans are the same. The traditional Company Pension Scheme used to be a **Final Salary Pension**, and it is largely these schemes that have folded as a result of an imbalance of funding input to pension output. Hence these schemes are being replaced with **Money Purchase Schemes** whereby what they pay out is directly limited to what is in them at any one time.

Extend this Money Purchase a stage further by removing the Company element, and you have what is now commonly known as the **Personal Pension Plan**. A Personal Pension belongs wholly to you as an individual, which makes it both portable and enduring. Portable because they can go with you wherever you work; and enduring because they are subject to your control rather than an employer's – past or present.

In its simplest form any Pension Plan is a certain type of **Savings Account**, where the intention is to set aside some of your excess Earned Income to provide a Retirement Income in the future. Pension Plans are also currently the most tax efficient Savings Scheme available in the UK. In favour of encouraging the nation to save for retirement, the Government afford full Income Tax Relief for whatever you put into your Pension Plan. So, for a **Basic Rate Taxpayer (20%),** a Personal Contribution of £80 will be uplifted to £100 by virtue of a £20 Tax Rebate. **Higher Rate Taxpayers (40% or 50%)** can reclaim a further £20 or £30 amounting to a total Personal Contribution of just £60 or £50 per £100.

A further advantage is that once a Pension Plan has been set up, the **Contribution Payment** becomes a routine habit, and has a good chance of surviving alongside any other financial commitments you may have.

The downsides are that you can only access your money from the **Age 55**; and even then you are limited as to what you can do with it.

A quarter of it can be taken as a **Tax-Free Cash Sum (25%),** if you can afford this luxury; but the rest you must take as **Retirement Income**. Most people choose to buy a conventional **Pension Annuity** to provide a secure income for the rest of their lives. Today however, there are some other very good alternatives, particularly a **Pension Drawdown Plan**, which is appealing to many more people by virtue of enhanced control, flexibility, and longevity.

All Pensions are a long-term investment in your own future; and should be considered very seriously. Ignore them at risk of your own peril!

Pension Savings Plans

Other than having some form of work-place Pension Plan, such as either a **Final Salary Scheme** if you are very fortunate, or an **Occupational Money Purchase Scheme**; the main alternative is an individual arrangement which commonly takes the form of a **Personal Pension Plan**.

A Personal Pension Plan is simply a statutory **Retirement Savings Scheme** approved by HMRC in respect of certain taxation arrangements. A Personal Pension is both owned and controlled by you as an Individual at all times throughout its lifespan, although other parties such as an employer can contribute to it on your behalf.

Personal Pension Plans are available to any UK Resident of any age, and you may have as many of them as you like, regardless of their past or current status. You can also start or stop your **Pension Contributions**, increase or decrease them, and have them remitted from any legal source, entirely at your own discretion. It is not uncommon for example, to stop making payments when money is scarce, or to increase your payments when either the need arises or your income increases. It is also quite common practice to pay in ad-hoc lump sums resulting from an annual bonus or business profit.

Pension Contributions

The main points now governing what goes in to your entire pension planning arrangements are:

- An **Annual Contribution Allowance** of upto 100% of your Earned Income subject to an upper limit of **£50,000** or upto £3,600 for people who earn less than this amount, including those with no earnings at all.
- A **Lifetime Contribution Allowance** of upto **£1.5M** which is built up from the above Annual Contribution allowances.

Your employer, if you have one, can also make Pension Contributions for you, but the total of all **Employer & Personal Contributions** are subject to the above limitations.

Whilst it is permissible to exceed these **Contribution Allwances**, it is rarely worthwhile because the excess amounts will incur significant **Tax Penalties** of upto **55%** rather than Tax Benefits.

Pension Investments

In most instances the primary purpose of a **Pension Investment Plan** is quite simply to build up a nest-egg from your Earned Income so as to provide a Pension Income when you retire.

Pension Contributions are usually converted into Investment Assets in the interest of being more productive until you need to realise them as a Retirement Income in cash again. The problem here for the average non-professional investor, is what to invest in, and how to do it?

There is a vast array of **Pension Investments** available today, including many highly credible and successful **Collective Investment Funds** both in the UK and worldwide. But with a base choice of more than 2,000 different Investment Funds alone, making the right choices can be overwhelming, and it constantly changes.

A Pension Plan won't work if nothing is put into it; but how well it works is largely controlled by how and where the money is invested.

Pension Retirement Benefits

All Pension Plans can now pay up to **25%** of the total value as a **Tax-Free Capital Sum**. If you were previously entitled to more than 25% you may still qualify for that higher amount. The Tax Free cash is paid directly to the Retiree to use as they wish – including using it to generate further Retirement Income.

The remaining balance of between **75%** or more, is used to provide some form of **Pension Income**, which is taxed at source by the Pension Scheme Administrator under the **PAYE System**. Therefore, in accordance with your total Personal Income, your Pension Income will be paid net of either **0%, 20%, 40% or 50% Income Tax.** The only good piece of news here is that once you reach your **Individual State Retirement Age**, you will have an enhanced Income Tax Allowance, and will no longer have to pay any **National Insurance Contributions**.

Traditionally, most people tend to buy a **Pension Annuity** with the proceeds of their Retirement Savings. All too often this happens simply because they do not otherwise exercise their wider options; and in other instances the decision is deliberate because a Pension Annuity is the only arrangement that will guarantee a certain income for the rest of their life.

The flip side of this is that unless the Annuity is set-up on a Joint Life basis, which comes at a considerable price in the form of less income for you, then your Pension Annuity will die with you. Furthermore, there is little or no scope for **Inheritance Planning.**

More recently however, many retirees are choosing **Pension Drawdown Plans** as a more attractive alternative to conventional Pension Annuities. Pension Drawdown Plans are simply a continuation of the original Personal Pension Plan, but having a slightly different structure by virtue of the fact that they are now in a decumulation rather than an accumulation status.

Pension Drawdown Plans enable retention of ownership by the Retiree because any residual **Capital Value** is retained within the Pension Plan rather than being spent on the purchase of an Annuity. This affords control and flexibility in favour of both the capital account and future income receipts. It also provides the opportunity for income tax mitigation by deferring benefits until a more favourable tax liability exists.

Furthermore, **Pension Drawdown Plans** typically yield considerably better results for any **Dependant's Benefits** following the death of the Pensioner. This is because the remaining **Capital Value** of the Pension Plan can be passed on to any chosen **Beneficiarie**s to be used as required.

Whatever your choices and preferences, the greater flexibility now available within the Pension Planning arena, should enable you to plan for a better retirement.

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Pension Benefits Summary Comparison

The following table summarises the main **Pension Capital & Income Benefit** options available to you at retirement:

Pension Annuity	Pension Drawdown
Guaranteed Contractual Benefits	**Variable** Pension Investment Benefits
Age **55 – 75** or Terminal Illness at any Age	Age **55 – 75** or Terminal Illness at any Age
A **Pension Annuity Contract** is purchased with the Capital Value of your Pension Plans to provide the following Retirement Benefits:	A **Pension Drawdown Plan** provides access to your Pension Capital as and when required to provide the following Retirement Benefits:
Upto **25%** of the Capital Value may be taken as a **Tax Free Cash Sum**. Any such amounts not taken are used to buy the Pension Annuity. There are no future options. **(1)**	Upto **25%** of the Capital Value may be taken as a **Tax Free Cash Sum**. Any such amounts not taken are preserved for future use as either Capital or Income. **(1)**
A **Retirement Annuity** is purchased with the remaining Pension Capital to provide a pre-determined and guaranteed Retirement Income at the best **Annuity Rate** available on the **Open Market**. All Pension Income is taxed as Personal Income under the **PAYE System**. **(2)**	A **Retirement Income** is withdrawn from the Capital Value of your Pension Drawdown Plan. Minimum Income is **Nil**. Maximum Income is **100%** of a comparable Single Life Annuity as determined by the Government Actuary Dept. (GAD). All Pension Income is taxed as Personal Income under the **PAYE System**. **(2)**
Annuity Options include: Fixed or Increasing Income, Payment Continuation Guarantee, Residual Capital Protection, and Joint Life Dependants Income. **(3)**	All above options remain open indefinitely; for both **You** and your **Beneficiaries**; and their values are dependent upon the **Market Value** of your Pension Plan. **(4)**
Once you have bought your Annuity, you cannot change your mind. Therefore you cannot recover your Pension Capital or amend the Income Benefits. Consequently there are **NO Inheritance Benefits**, with the exception of a **Joint Life Annuity** or **Capital Protected Annuity**, nor are there any **Inheritance Taxation** issues.	On death, the residual balance of your Pension Plan is passed on to the **Beneficiaries** of your **Estate** in accordance with your **Will.** Some Income Death benefits may be subject to a **25%** Taxation Liability and some Capital Death Benefits at **55%**.

Notes:

(1) The more you take out as a Tax Free cash Sum, the less will be available to generate an ongoing Pension Income.

(2) Your Annuity/Pension Drawdown Provider will deduct Basic Rate Income Tax @ 20% under the PAYE System, so that your Net Income will amount to 80% of the Gross Value.

(3) With the exception of a Payment Continuation Guarantee of upto 10 Years, all other otions carry a considerable price by way of a much reduced Pension Income which may be upto 50% less than a Single Life Annuity.

(4) Your chosen Beneficiaries, which may include any number of people, may Inherit the Full Residual Balance of your unused Pension Plan. If this happens prior to your Age 75 there are no further Tax Liabilities; but from Age 75 onwards any Continuing Income is taxed at 25%, and Capital at 55%.

Products and Providers

With such a vast array of choices available today, how do you decide what's right for you? What's the best solution; and who's got the best product?

We begin by considering the generic, non commercial factors as follows:

- Ownership - to whom does it ultimately belong?
- Purpose - is it designed to do the job required?
- Benefits - is it most likely to produce the right results?
- Control - who's in charge of making any changes?
- Cost - is it good value for money?
- Tax Efficiency - is it as tax efficient as possible?
- Administration - is it simple enough to maintain?

Generic Advice

A **Pension Plan**, as stated earlier, is a special kind of savings scheme with a certain purpose. Pension schemes may be set up on either a **Defined Benefit** basis whereby the final outcome is pre-determined – irrespective of the cost; or on a **Defined Contribution** basis whereby the cost is known but the benefit is not.

Not surprisingly a **Final Salary Pension Scheme** (Defined Benefit) is almost always the preferred choice. However, as a result of rising costs and diminishing returns they are a rare and disappearing luxury today.

The next best option for any potential Pensioner would be a **Money Purchase Scheme** (Defined Contribution) funded entirely or in part by an employer. Whatever the final outcome might be, at least the cost is shared by another party. In either of the above cases, if you're offered membership of a **Company Pension Scheme** which includes **Employer Contributions**, then the answer should probably be yes!

The fall-back option is a **Personal Pension Plan** funded and wholly owned by you. It works by building up a Pension Fund using your Contributions, which are then enhanced by virtue of Investment Growth. The value of your Pension Fund at Retirement will therefore depend upon the level of **Gross Contributions**, **Investment Growth Rates**, and **Policy Charges**.

Retirement Income values will depend upon the age at which you retire, how much you take as a Tax-Free Cash Sum, and the Retirement Income arrangement that you choose.

Specific Recommendations

If having established, by virtue of your own circumstances, that your overall Retirement Planning arrangements should include a **Personal Pension Plan**, we would then consider the following specific criteria in our search for the most suitable product provider:

- Financial Strength of the Provider
- Product Construction
- Investment Selection
- Costs and Constraints
- Transactional Functionality
- Quality of Service
- Terms & Conditions

Investment Platforms

An **Investment Platform** allows for multi-product management and multi-asset investment control - all within a single umbrella Client Account. They are usually administered online, and enable full Transactional functionality, together with Real-Time Reporting facilities. Furthermore, by consolidating all your Investment and Pension Investment Accounts within a single Holding Account, you will benefit from enhanced management, efficient administration, and reduced costs.

Investment Platforms usually also provide some powerful **Risk & Reward Profiling** tools, and **Investment Research & Selection** tools, which are vital in determining appropriate investment decisions.

There is usually a **Fund Supermarket** at the core of an Investment Platform which make Collective Investment Funds both readily accessible, and often less expensive. Subject to very minimal investment levels, an Investment Platform usually removes any initial entry barriers; and the price advantages afforded by the buying power of Platform Providers, may be used to offset any additional Platform Charges associated with the provision of the Client Account.

Please feel free to ask us for any clarification or further information about your Pension Planning. Of all the products we deal with, Pensions are by far the most complex!

We look forward to helping you further in this regard.