New Pension Freedoms Case Study - The Risks of high levels of income withdrawals

From the 06 April 2015, as a result of the new pension freedoms, you can decide exactly how much income to take from your pension (withdrawals are subject to tax). You need to understand that this new freedom comes with responsibility and you will need to ensure that you do not run out of money later on in retirement.

The following case study is for illustration purposes and is not based on a real life example. However, it is designed to highlight the dangers of high levels of withdrawals from your pension fund.

If you make high levels of income withdrawals from your pension fund, your fund could be significantly, if not completely eroded, meaning that you could have little or nothing remaining to provide an income for you or your spouse later in retirement.

Example – a healthy 60 year old male with a £120,000 pension fund invests in our Cash Retirement Account, takes his maximum tax free cash lump sum at outset of £30,000 and takes income of £10,000 per annum, paid monthly in advance. At the end of year five, his maturity amount is £44,338.

Assuming interest rates have not changed, were he then to invest in another five year Cash Retirement Account and maintain the same annual income of £10,000 per annum, his fund will have been completely exhausted prior to maturity.

Alternatively, had he purchased a lifetime annuity at outset, the income available would have been £3,967 per annum, payable for life*.

Were he to invest his £44,338 maturity amount, at the end of year five, in a lifetime annuity, the best income available would be £2,209 per annum, payable for life**.

As this case study highlights, high levels of income withdrawals can quickly exhaust a pension fund and you need to consider what will happen if you live longer than expected and be willing to manage the risks. The main way of doing this is to take a lower level of income.

NOTES

*The annuity income quoted is the best rate available on the open market for a 60 year old, non-smoker, level income, no death benefits and paid monthly in advance (current rates as at January 2018).

**The annuity income quoted assumes rates remain unchanged and are the current best rates available for a 65 year old, non-smoker, level income, no death benefits and paid monthly in advance (current rates as at January 2018).

IMPORTANT NOTE

This case study is an example intended to highlight the risks of high levels of income withdrawals. You should not take, or refrain from taking, any action based on this information. Tax treatment can change and depends upon your circumstances. Please remember that taking money out of a pension will impact your standard of living later in retirement. This information is not advice and if you are unsure about the suitability of an investment, you should seek Independent Financial Advice.

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