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CLEVER RETIREMENT STRATEGIES

How to influence the income you'll receive in your retirement

On 10 July 2014, the Office for Budget Responsibility warned that many of us might not be eligible for a State Pension until we reach the age of 70. That's the minimum age the Government will be able to afford to pay our pensions by 2063 if it is also to stop the national debt spiralling out of control.

This milestone could be reached as soon as 2037 – meaning that some people in their late 40s today may have to work to age 70. And if the population ages more quickly than currently forecast, the State Pension age could increase to age 75 in 2064. By then, the UK's official budget watchdog says there could be more than one million people aged over 100 in the UK.

LIFE EXPECTANCY INCREASING

With life expectancy increasing at a rapid rate, you will probably live for longer than you think and, as such, your pension income will need to last longer. Therefore, it is essential to eke out as much income as possible from your retirement savings and, with interest rates at historical lows, this is no easy task.

It is important to remember that your pension income will not just be a function of the pension vehicle you choose – whether this is an annuity, income drawdown or another arrangement. You can also influence the income you receive in retirement by making clever use of different retirement strategies.

THREE RETIREMENT STRATEGIES TO CONSIDER

1. DEFER YOUR STATE PENSION

Retirement should be a gradual phasing in of income to free up spare time – it does not necessarily have to mean that you stop working or earning. There is no reason why you have to stop working or claim your State Pension when you reach State Pension age – currently 65 for men and 62 for women.

If you put off claiming your State Pension, you can either earn extra State Pension or benefit from a one-off lump sum payment. If you have not yet claimed your State Pension and you want to put off taking it up, you do not need to do anything. Those already drawing their State Pension, but wanting to stop claiming it to earn more income, will have to contact their pension centre.

It is, however, worth noting that the terms for deferring your State Pension are very different for those who reach State Pension age before 6 April 2016 compared to those who reach it afterwards. For those who reach State Pension age before 6 April 2016 (men aged 64 or more at April 2015 or women aged 62 or more at April 2015), the rate of deferral is very generous – 10.4% per annum plus the inflationary increases. In comparison, the lump sum alternative may be poor value for money.

For people reaching State Pension age after 6 April 2016, the rate of deferral at the time of writing this article had not been set but is expected to be 5% per annum plus inflation, and there will be no lump sum alternative.

2. USE EMPLOYMENT TO TOP UP YOUR PENSION

If you are employed, there are a number ways in which you can top up your pension:

SALARY SACRIFICE

Salary sacrifice involves giving up some of your salary in exchange for payments into your pension. This will not only increase your pension contributions and overall pension fund but can also mean savings on income

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tax and National Insurance. You will receive tax relief, depending on the tax band you fall into. It is, however, worth remembering that a reduction in your salary could impact your ability to secure a mortgage, as banks and building societies use income to decide on loan eligibility.

BONUS SACRIFICE

In a similar way to salary sacrifice, you can make potential tax savings by using bonus sacrifice to pay into your pension plan. If you are a high earner, chances are that you receive a basic salary as well as bonus payments. Typically, you will be offered the chance to sacrifice some of this bonus and instead have that money paid into your pension scheme.

This is arguably one of the most tax-efficient ways of getting extra money into your pension plan, since you are not taxed on the amount of bonus that you give up. Your total income is reduced and therefore you are only taxed on the income you actually receive. The part that goes into your pension is not taxed as it is instead an employer contribution. This means you save on income tax and National Insurance.

Furthermore, your employer will not pay National Insurance on the amount of bonus given up – usually at 13.8% – and if they wish, they can pass some or all of this saving back to you.

COMPANY SHARE PENSIONS

Those who hold shares in employer share schemes can place these within a self-invested personal pension (SIPP) and benefit from the tax relief. You can either sell the shares and invest proceeds into your SIPP or move the shares into the SIPP. Once the shares are transferred into a SIPP, any future growth and dividend payments will be tax-efficient.

3. BUILD IN INFLATION PROTECTION

If you are still saving for retirement, it is important that you keep increasing the amount you pay into your pension each year. If you don't, inflation means that your monthly contributions will be worth less every year.

If you expect inflation to rise, then consider investing your pension fund in higher-risk assets such as equities, as rising inflation will eat away at the more cautious investments such as cash, fixed interest and low-risk funds. You will have to take into consideration how many years it will be before you retire and whether you can afford to take the risk of investing in these assets.

Once you reach the point of retirement, you can inflation-proof your income by opting for an inflation-linked annuity, although these usually have a low starting level of income.

Alternatively, you can look at using a drawdown arrangement, usually making use of a multi-asset approach to investment that aims to allow income to be withdrawn while maintaining the real value of your investments.

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Under this approach, you won't have a guaranteed income, but you retain ownership and control of your assets while staying abreast of inflation if the investments perform well. However, it is sensible to make sure your essential expenses are covered with a source of secure income where possible.

CLOSER TO RETIREMENT

Retirement may be a long way off for you at the moment, but that doesn't mean you should forget about it, and as you get closer it makes sense to have a clearer idea of what you'll need to live on in the future and what your income might be.

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PROFESSIONAL FINANCIAL ADVICE YOU CAN TRUST

The sooner you start to plan for your future, the easier it is to build up the kind of money you need to enjoy the life you want. To discuss your options, please contact us for further information about how we can help you build the pension income you want.