Planning ahead is vital to avoid volatility in the markets hitting your pension pot

Whether it's a week or a year until you retire, there's plenty to think about, **writes Jeff Salway**

Retirement

IF YOU are on the brink of retirement, the latest plunge in stock market values couldn't have happened at a worse time.

Thousands of people with pension investments still exposed to equity markets as retirement nears have seen the value of their savings ravaged by market falls. The damage has been exacerbated by a decline in annuity rates, meaning those using their pension fund now to secure a regular income for their retirement will get less than if they had retired just a few weeks ago.

The turbulence has offered a painful reminder that most people's pensions are now at the mercy of the markets, with final salary schemes now relatively rare in the private sector.

Gordon Wilson, managing director of Edinburgh-based Carbon Financial Partners, said: "If you don't have a financial plan that builds in some protection against stock market downturns then you could be forced to make some difficult decisions."

So what can you do if you're planning to retire in a month's time, or in the next six months or year? Here we set out your options as the countdown to retirement reaches its final stages.

ONE YEAR TO GO

This is the time to take stock, work out what you've got and what you can do to improve it. First, find out what your pensions are worth. You can get a forecast of your current state pension entitlement and the likely figure at retirement from the Pension Service (0845 3000 168 or www.thepensionservice.gov.uk). Also contact your pension provider(s) to get a projection of the value of your fund at retirement. You may well have pensions with previous employers that you've lost track of. The Pension Tracing Service (0845 6002 537) can help you find them. It has information on more than 200,000 personal and occupational pension schemes and needs surprisingly few details to track one down.

Once you've got an idea of the pension you can expect you can think about how it fits in with your plans.

Paul Lothian, right, director of Verus Financial Planning in Dundee, said: "Calculate the additional contributions that are required to fund any retirement income gap. If this cannot be afforded, make economies or revise expectations of retirement income or retirement age. Also consider consolidating your pension arrangements."

Make sure your investments reflect your situation by minimising the risk to which you're exposed, something you will ideally have done prior to this point, he added.

"Reduce your exposure to equity and property funds to 0 per cent and replace it with fixed interest funds," he said.

One thing you certainly should not do is make short-term investment decisions in the hope of making up lost ground.

Wilson said: "One year is very short-term and impossible to predict. Take the emotion and speculation out of the equation and deal with the hard financial facts. Even with recent falls you may have enough, so there's no need to panic – just put plans in place."

But what can you do if your pension looks like it's going to be smaller than you'd expected?

Wilson said: "Firstly, properly understand what you've got, how much risk you're taking and when this is likely to provide enough money for you to retire.

> "Boosting contributions through salary or bonus sacrifice is very tax-efficient"
> *David Gow*

"If this takes you to a retirement date later than you'd want, you either need to save more money into your pension or take more risk to give you the opportunity to achieve higher returns, bearing in mind that if your investments can go up more in value they can also come down more."

David Gow, a chartered financial planner at Acumen Financial Planning in Edinburgh, suggested making extra pension contributions if possible.

"Boosting contributions through salary or bonus sacrifice is very tax-efficient, particularly for higher-rate taxpayers," he said.

For example, if you're on a basic salary of £60,000 you could reduce your salary by £17,525 – enough to get you within the basic rate threshold – in return for extra pension contributions from your employer.

"You would save £350.50 in employee National Insurance contributions, while your employer would save £2,418.45," Gow said.

"If your employer agreed to pass their National Insurance saving on to you, an employer pension contribution of £20,293.95 could be made at no extra cost to your employer – £2,768.95 more than the salary you have given up."

If you can't save enough to give you the pension you need, delaying your retirement could be something to begin thinking about.

SIX MONTHS TO GO

Most people buy an annuity at retirement to convert their pension pot into an income. But you should start researching your options carefully, because taking the first deal your pension company offers could be a costly mistake.

With a gap of around 20 per cent between the best and worst annuities available, you can give your retirement plans a massive boost by finding the best deal on the market.

You can improve it further if you're a smoker or in ill-health – even if it's a minor condition – by looking for an enhanced annuity, where the income is higher on the basis that the payout period is likely to be shorter.

Conventional fixed annuities are the au-

Law offers a helping

A LITTLE-known change in the Finance Act 2011 could help people whose pensions have been hit just before retirement.

The change allows your pension pot time to recover as well as mitigate inheritance tax (IHT), charged at 40 per cent on assets worth more than £325,000 (or £650,000 per couple).

The logical approach to IHT planning has always been to finance living expenses in retirement from non-pension assets up to age 75: these assets (unlike pension funds) are liable to IHT, so consuming them would potentially lessen exposure.

Until now, however, there has been a significant drawback to such a strategy: the UK IHT code contains an anti-avoidance

hand when considering inheritance tax

provision, which basically entails that not drawing on pension assets could be deemed a transfer of value for inheritance tax purposes, if it has the effect of reducing your estate.

The Finance Act 2011, which came into force last month, means this provision will no longer be an issue.

That means if you're cash rich and have significant non-pension assets you could live on these without fear of IHT issues, and allow pension funds to recover from the current slump.

You should draw on non-pension income and capital to fund living costs until age 75 and leave pension funds untouched. This will give your pension fund time to recover, and will reduce the value of your taxable assets.

If you die before the age of 75 and haven't drawn benefits from a pension, the entire fund can be paid out as a tax-free lump sum to beneficiaries.

However, if you die at or after age 75, your beneficiaries will be hit with a tax charge of 55 per cent if you take the pension savings as a lump sum.

So, reverse the approach when you reach age 75, so that living expenses come from pensions. Don't risk the 55 per cent tax charge on what would otherwise be tax-free cash.

David Gow is a chartered financial planner at Acumen Financial Planning in Edinburgh

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Recent volatility in stock markets worldwide will have hit pensions, but with careful advance planning you should be able to minimise the impact this has on your finances

tomatic choice at retirement for the vast majority of people, but with the decline in annuity rates tipped to accelerate over the coming months more people are looking for other ways of securing their retirement income.

Annuities with a link to inflation are increasingly popular, as are products that combine a guaranteed income with some potential for growth. If you have a good amount of savings and other income to fall back on, you could also consider drawdown, where your fund remains invested and you take cash from it in tranches.

Wilson said: "If you're lucky enough to be in this position, your chosen retirement age might be a bit of a red herring as your pension fund could remain invested for more than 20 years or more after you retire from work.

"This means that a longer-term view can be taken and there may be no need to protect any gains in the lead-up to retirement."

Lothian advised shifting your investments into cash at least three months before your planned retirement date.

"Get another update of your fund values and benefit statements and seek independent financial advice to explore and compare your options, including establishing the level of income available from various annuity types and also the relative merits of the alternative approaches available," he said.

ONE MONTH TO GO

For every five weeks you defer your state pension you can boost your weekly pension payment by 1 per cent. If you defer for at least 12 consecutive months you qualify for a lump sum plus interest of the base rate plus 2 per cent. If you plan to do this you need to tell the Pension Service (0845 3000 168). Similarly, tell your employer if you intend to work over state pension age so that your National Insurance contributions are reduced.

Get in touch with your pension provider to find out how much your pension is worth and how they will pay it. Tell them if you intend to defer taking your pension benefits.

Look again at the steps above – review your plans and the steps you've taken, bearing in mind any change in circumstances.

ONE WEEK TO GO

Ideally you'll be well prepared by now but, as many people have discovered to their cost lately, economic and market volatility has a habit of throwing a spanner in the works.

If at this point you still have money exposed to the stock market but you're planning on taking your pension pot when you retire, market falls can cause massive damage to the value of your fund. You should have decided by now how you'll take your pension fund, but take time to review your decision. If you're buying an annuity, remember that shopping around is essential.

This is a time when independent financial advice is invaluable, as the decisions made now will have a profound impact on your finances for the rest of your life.

To find a financial adviser near you, visit www.unbiased.co.uk. If possible, opt for a fee-based adviser with certified or chartered qualifications (or both); the short-term cost of this should be outweighed by the long-term savings.