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## INCOME DRAWDOWN VERSUS ANNUITY PURCHASE

This fact sheet looks at the advantages and disadvantages of income drawdown compared with annuity purchase. **The Pensions Advisory Service is unable to give individual specific advice and you should seek independent financial advice if you require further assistance.**

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### Income Drawdown

#### Advantages of Income Drawdown

##### Flexible payments and control

- Income drawdown allows greater flexibility than annuity purchase, since the level and frequency of income payments can normally be varied to suit your needs.
- Income payments can stop at anytime because there is no minimum income limit.
- In addition to regular income, it is normally possible to choose to receive one-off payments.
- The opportunity to take 'flexible drawdown.' Please refer to our fact sheet 'Spotlight on the new flexible drawdown rules'.

##### Funds remain invested

Funds designated for income drawdown purposes remain invested and continue to benefit from any fund growth.

##### Tax-free cash sum without a regular income

There is no requirement to take income, so you can take part of your fund as a tax-free cash sum (up to 25%) leaving the remainder of the fund to benefit from any fund growth.

##### Death benefits

Your husband, wife, registered civil partner or dependant can normally continue with income drawdown payments, buy a lifetime annuity or take the remaining fund as a lump sum less a 55% tax charge. Please refer to our fact sheet 'Spotlight on tax and lump sums paid on death – income drawdown'.

##### Delaying annuity purchase

Delaying annuity purchase may mean that annuity rates will improve with the member's age.

#### Disadvantages of Income Drawdown

##### Fund depletion

The pension fund could be depleted by poor investment performance, by taking too much income out of the fund or by the effects of charges.

Fund depletion could result in a significant reduction in income and eventually no assets left from which to draw an income.

##### Investment risk

As your fund will remain invested, its value will continue to fall or rise in line with the underlying investments.

##### Delaying annuity purchase

There is no guarantee that delaying annuity purchase will give a better pension income. Annuity rates could be worse.

Your income is not guaranteed and may vary depending on fund performance.

##### Advice

The cost of advice needs to be considered with income drawdown. You must be prepared to review your pension fund and income on a regular basis.

The potential risks associated with income drawdown mean that many advisers suggest it is not really suitable for funds below £100,000 or where this is your only source of income.

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## Annuity Purchase

### Advantages of Lifetime Annuity Purchase

#### Guaranteed income

- Lifetime annuities give a guaranteed income for life, irrespective of personal circumstances and without the risks inherent in income drawdown.
- You may get a higher annuity through an impaired life annuity or through 'smoker rates'.
- There is no investment risk. You may choose to have protection against inflation by selecting an annuity which increases each year.

#### Phased annuity purchase

If you have a larger fund, phased annuity purchase in combination with income drawdown may allow you to take advantage of any improvements in annuity rates.

A phased annuity plan is usually split into 1000 or more segments. Your income requirements are assessed on a yearly basis and one or more segments are used to buy an annuity if required.

You do not have to disinvest segments each year, which gives you flexibility regarding to the amount and timing of income taken.

The remainder of your pension pot remains invested, with growth depending on the type of funds which you have chosen.

### Disadvantages of Lifetime Annuity Purchase

#### Loss of flexibility

Once started, the annuity cannot be altered.

#### Death benefits

When you purchase an annuity, you have the choice of whether to select a guarantee period of 5 or 10 years. This means that should you die within that time the pension will continue to be paid until the guarantee period ends. The payments can continue to be made to your spouse or someone who is financially dependent on you. Otherwise payments will be made to your estate and distributed according to your will.

If you have a value protected annuity, a lump sum will be paid giving a return of the purchase price to buy the annuity, less gross annuity instalments paid to you, less a 55% tax charge.

When you choose your annuity, you will have the option to use your pension pot to provide an annuity to your spouse after you die. The pension available in this way is usually at half the rate of your annuity. This option will, however, reduce the annuity you will get.

If you have not chosen any protection for your dependents, benefits will cease on your death.

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## About Us

The Pensions Advisory Service has been providing help and guidance to members of the public on pension matters since 1983 either by telephone or written advice. We can also help people who have a pension complaint or dispute.

Our service is free and sustained by a nationwide network of volunteer advisers, who are supported and augmented by technical and administrative staff based in our London office.

#### Contacting us

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