WEALTH OF ADVICE

PENSION INCOME OPTIONS

ANNUITIES EXPLAINED

Your straightforward guide to understanding how annuities work, the options available, and how they can provide a guaranteed income in retirement.

IMPORTANT INFORMATION.

We have written this guide to help you understand more about your retirement options and it is not personal advice.

Your retirement income will usually be generated from your pension which can be accessed from age 55 (rising to 57 from 2028).

We recommend you take care to understand the options available to you with your pension and check that your chosen option is the best fit for your circumstances.

The information in this guide is correct as of April 2026. UK tax rules can change at any time and its impact depends on your circumstances.

We are Wealth of Advice, authorised and regulated by the Financial Conduct Authority, reference number 563909.

ENQUIRIES@WEALTHOFADVICE.CO.UK

WWW.WEALTHOFADVICE.CO.UK

0191 384 1008

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SINCE 2011

WHAT IS
AN ANNUITY?

Using a lump sum payment, you can purchase an annuity which will provide you a guaranteed income over a set period.

If a life annuity is selected, it does not matter how long you live for, the income is guaranteed to be paid.

The income generated is not impacted by stock market movements (unless an investment annuity is selected).

If your existing provider offers an annuity, you can purchase this. However, it pays to shop around on the open market to ensure you receive the best value for your money.

The annuity rates offered by providers will vary. Certain factors will impact the rate you are quoted, which we cover in more detail later.

The income from an annuity is taxable, like a salary from employment.

It's also worth mentioning that once you purchase an annuity, you are locked in and it cannot be cancelled or changed.

WHAT AFFECTS
YOUR INCOME AMOUNT?

The factors that affect the annuity rate you may receive are as follows:

Size of your pension

The more of your pension you use to buy an annuity, the higher the income that will be generated.

Age, Health & Lifestyle

As a rule of thumb, the older you are, the higher the annuity you will receive. If you disclose unhealthy lifestyle options or underlying health conditions, this can also lead to a higher annuity. This can include things such as units of alcohol consumed and your height and weight which sets your Body Mass Index. Some providers may allow you access to an enhanced annuity rate.

Annuity Rates

Annuity rates determine the income you receive. The rates change all the time as they are linked to gilt yields (returns made on government bonds) and are sensitive to interest rate changes. If yields are high, annuity rates are high. If yields are low, you guessed it, rates are lower.

Income Frequency

You can choose to receive income monthly, quarterly, bi-annually, or annually. This can also be paid in advance (up front once the annuity is set up) or in arrears (at the end of the selected payment period). The longer you go without receiving an income, the likelihood is that your annuity will be higher.

UNDERSTANDING YOUR
INCOME OPTIONS

Single or Joint Life

You can select an income to be paid to you only, which stops on your death (single), or you can select an income that continues to pay to a selected joint party which will continue after your death (joint).

Employment Earnings

Another form of protection, this ensures the original value used to purchase the annuity less any income paid to you is passed to your beneficiaries.

Level or Increasing

You can select an income that is fixed for life or for the fixed term (level), or an income which is lower at the outset but increases in line with inflation or by a specified percentage (increasing).

Guarantee Period

Selecting a guaranteed period will guarantee the annuity will continue to be paid for that length of time even if you die during that period For example, if you select a 30-year guarantee period on an annuity and you die after 2 years, the payments will continue to your nominated beneficiary for a further 28 years.

THE DIFFERENT TYPES OF ANNUITY

Lifetime Annuity

An income paid for life to the parties to the annuity. The income is guaranteed to be paid until death of the last annuitant. Excellent for someone with no appetite for investment risk.

Fixed Term Annuity

An income paid for a specific term usually ranging from 3 to 25 years. Providers in this market are limited.

Investment Linked Annuity

These annuities carry more risk than lifetime and fixed term annuities as the income rises and falls in line with the value of the investment you have elected to buy. This can be for life or a fixed term but either way, the income you get is not guaranteed.

Purchased Life Annuity

This can be purchased with money that is not in your pension or you can use the tax-free cash from your pension to secure additional income for retirement. These are largely like the annuities described above, but the tax treatment is slightly different.

Each payment is made up from part of the fund invested (capital) plus the part that is interest.

Income tax is not levied on the capital element. Tax is only paid on the interest element.

Enhanced Annuity

If you suffer from certain health conditions or have adopted a specified lifestyle, a provider may offer you an enhanced annuity. This means the income you receive will be higher than the standard rates as they expect to pay out the income over a shorter period as your life expectancy is calculated to be lower than an individual with no health conditions.

A CASE STUDY

John came to Wealth of Advice with a pension pot of £830,000 at age 59.

JOHN'S GOAL

John's goal was to find a retirement income option that would provide stability in retirement, but with the ability to adjust his income and to leave something behind for Anne, his wife, and their two children when he passes away.

OUR RECOMENDATION

Our recommendation was to use a combination of pension options for their retirement plan, by purchasing an Annuity with part of John's fund and moving the rest into Income Drawdown.

By using £200,000 of his pension pot to purchase a Single Life annuity with a 30-year guarantee, John was able to secure a guaranteed income of £11,300 a year.

John and Anne would use this money to cover essential expenditure, while the remaining £630,000 would stay invested, using Income Drawdown for any additional income or lump-sum requirements.

As John has kept some of his pension fund in Income Drawdown, he is able to leave the remaining funds to his loved ones when he passes away.

As financial planners, we regularly review John and Anne's finances and manage their investments to make sure they are still on the right track with their retirement and that the income still suits their needs.

UNDERSTANDING ANNUITY RISKS

Once in payment, an annuity cannot be stopped or amended.

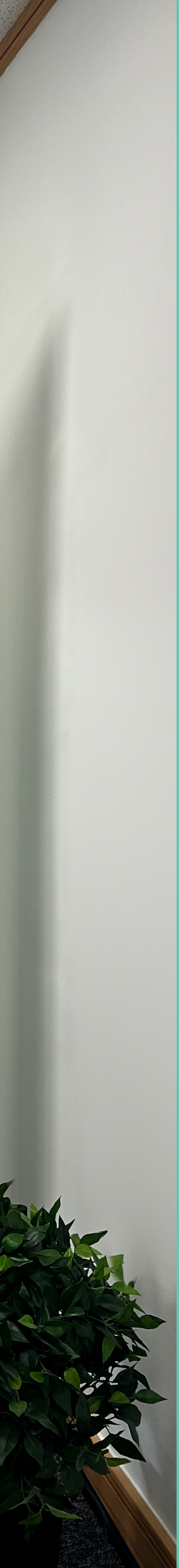
Selecting either joint, increasing or a guarantee period will reduce the value of the annuity payable to you.

Usually, there is no ability to leave a lump sum from your pension to beneficiaries once it's been used to purchase an annuity.

If you choose to receive a level income and inflation increases, your money will not stretch as far. Selecting an increasing annuity will reduce the initial level of income.

You may get back less than you have paid in, depending on how long you live.

The income is taxable and cannot be amended to reflect your personal position if this changes.



WHAT HAPPENS WHEN YOU DIE?

If you have a single annuity product with no added features, the income will cease upon your death.

DEATH BEFORE AGE 75

Income from a joint annuity will be paid tax free and will end upon the death of the second person.

Income paid under a guaranteed period will be paid tax-free and will end once the guaranteed period expires.

Lump sums or income issued under a value protected arrangement will be paid tax-free.

DEATH AFTER AGE 75

Income from a joint annuity will continue to be paid at the survivor's marginal rate of income tax and will end upon their death.

Income paid under a guaranteed period will be paid to the beneficiary at their marginal rate of income tax and will end once the guaranteed period expires.

Lump sums or income issued under a value protected arrangement will be paid subject to the beneficiary's marginal rate of income tax.

INHERITANCE TAX CONSIDERATIONS

From April 2027, pension funds will be included in an individual's estate for Inheritance Tax (IHT) purposes.

Benefits being passed to a spouse or civil partner will qualify for spousal exemption.

Death-in-service benefits, dependants' scheme pensions, survivors' pensions under joint life annuities and death benefits to qualifying charities will not be included.

THINGS TO CONSIDER

Annuities do provide a guaranteed income for life or fixed term and relieve the worry about your money running out. However, once you've selected to purchase an annuity and the cancellation period passes, there is no option to cancel, so think carefully before you commit.

An enhanced annuity can be attractive for the increased income that can be generated. However, if you have a limited life expectancy, a guaranteed income option may not be the right choice for you.

Some older pension policies offer a guaranteed annuity rate when you reach the selected retirement age of the pension scheme – also referred to as GARs. These can offer valuable benefits that can be hard to match from the open market.

Once you have purchased an annuity, in most cases, you can continue to receive tax relief on pension contributions up to the Annual Allowance of £60,000. In comparison, purchasing an investment-linked annuity or accessing a taxable income from an income drawdown plan will trigger the Money Purchase Annual Allowance which reduces the Annual Allowance to £10,000.

Any income generated by an annuity will affect any state benefit entitlement.

You can mix and match your retirement income options and it is important that you understand these options that are available to you. Seeking financial advice can help you plan your retirement income journey.

WoA

WE'RE ALWAYS LOOKING TO IMPROVE AND GROW - WHETHER IT'S OUR CLIENTS' INVESTMENTS OR OUR OWN QUALIFICATIONS.

THE ADVANTAGES OF
FINANCIAL ADVICE

Annuities can play an important role in creating financial security and peace of mind in retirement, but they're not the right solution for everyone. Choosing when to buy an annuity, what type to select, and how it fits alongside your other retirement income sources requires careful consideration.

At Wealth of Advice, we believe retirement planning should be built around your goals, circumstances and aspirations. Whether you're approaching retirement, reviewing existing pensions, or considering your annuity options, our experienced advisers can help you make informed decisions with confidence.

GET IN TOUCH WITH US

enquiries@wealthofadvice.co.uk

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