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FACTSHEET

Brexit

Existing pension commitments that might have to be re-examined

During the referendum campaign, the Prime Minister, David Cameron, said the so-called 'triple lock' for state pensions would be threatened by a UK Brexit. In their 2015 election manifesto, the Conservatives promised to extend the triple lock on state pensions – a guarantee that they rise every year by at least 2.5%, or the rate of inflation, or growth in earnings if it is higher until 2020.

NATIONAL INCOME

While pensioner benefits were a 'policy priority' and he was committed to honouring manifesto promises, the Prime Minister said £90bn was spent on it every year and it was among many existing commitments that might have to be re-examined in a post-Brexit climate. Again, this assumes a poorer economy and lower national income going forward.

If economic performance deteriorates, the Bank of England could decide on a further programme of quantitative easing as an alternative to cutting interest rates, which would lower bond yields and, with them, annuity rates. So anyone taking out a pension annuity could receive less income for their money.

WHAT COULD THE FUTURE HOLD FOR PENSIONS OUTSIDE THE EU?

DRAWDOWN

For many people with money invested in 'income drawdown', they should do nothing unless they have to. Income drawdown is a way of using a pension pot to provide a regular retirement income by reinvesting it in funds specifically designed and managed for this purpose. The income received depends on the fund's performance and isn't guaranteed for life.

Up to 25% (a quarter) can be taken from the pension pot as a tax-free lump sum. The rest is moved into one or more funds that allows for an income to be taken at a time when it suits. Most people use it to take a regular income. The income received may be adjusted periodically depending on the performance of the investments.

There are two main types of income drawdown:

- Flexi-access drawdown – introduced from April 2015, where there is no limit on how much income can be taken from drawdown funds
- Capped drawdown – only available before 6 April 2015 and has limits on the income that can be taken out; if someone is already in capped drawdown, there are new rules about tax relief on future pension savings if they exceed their income cap

WIDER ECONOMY

As we have seen post the Brexit result, there is likely to be a period of volatility in the markets and uncertainty in the wider economy. In these conditions, acting in haste is unlikely to serve well for many people unless there are good reasons for doing so.

For people many years away from retirement and making regular savings, unless Brexit has impacted on a change in their current circumstances it will be prudent to keep saving. It's also worth remembering that when markets fall, investments are acquired at a lower price, resulting in the opportunity to gain when markets rise.

ANNUITY RATES

It is likely that for the foreseeable future, annuity rates will continue to remain at their current low levels. An annuity is a product available for retirees and offers an income for life, bought at retirement with all or part of a person's pension savings.

The current returns available reflect movements in interest rates, and since Brexit the money markets have signalled further lower long-term rates. Gilt yields and annuity rates have been falling steadily over the past year and could reduce even further.

NEWLY RETIRING

Cuts have already taken place following falls in the yields on bonds issued by the Government in the wake of the EU vote, and more falls in annuity rates are likely to follow. On Monday 27 June, some pension companies began to cut the amount they will pay people who are newly retiring.

If someone is considering using their pension to purchase an annuity to fund their retirement, they should obtain professional advice sooner rather than later.

PENSION SAVINGS

For those wanting to delay purchasing an annuity but needing to draw on their pension savings, if appropriate they could draw an income from their funds using a drawdown arrangement.

In the longer term, there is a possibility that some of the stringent EU rules on the amount of capital that insurers have to hold to support their annuity may be relaxed ever so slightly, and this should be good for annuities.

FINAL SALARY PENSIONS

There are currently over 11m people that have defined benefit pensions (final salary schemes). Many people may have one if they currently work or have worked for a large employer or in the public sector.

A defined benefit pension scheme is one where the amount paid is based on how many years a member works for an employer and their salary earned. These schemes pay out a secure income for life which increases each year.

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SUFFICIENT MONEY

An employer contributes to the scheme and is responsible for ensuring there's sufficient money at the time of retirement to pay a pension income to the member, and there is no reason to expect any instant effects of the Brexit vote on such schemes.

Once earned, the benefits due from a defined benefit pension scheme cannot be changed without members' approval unless the company concerned goes out of business.

ECONOMIC GROWTH

However, if interest rates stay lower for longer and economic growth is weak, some schemes' funding could be put under more pressure.

It is possible that some defined benefit pension schemes may think about passing more of the cost on to members by increasing their contributions. But any change is unlikely until each scheme's next official valuation, which happens once every three years.

STATE PENSION

As the state pension is 'unfunded', it's not backed by an investment fund, which means it is not affected directly by movements in the financial markets. Any potential effects of Brexit on the state pension is likely to occur in the longer term.

However, a severe post-Brexit recession could put pressure on the tax revenues that are needed to pay the state pension.

ALREADY RETIRED

Any changes to the state pension are more likely to affect those who have not yet retired rather than those that have already retired. One significant state pension change in the future could be an impact on the 'triple-lock', which now looks more uncertain following the EU vote.

The triple-lock guarantees that the state pension will rise by the higher of prices, average earnings or 2.5%. Before the referendum, David Cameron warned this 'special protection' would be under threat if there were a 'big black hole' in the economy following a Brexit vote.

Pension saving should still remain a priority, especially given that the tax relief currently available on contributions may not be here forever.

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