Retirement Options

At the time you take your retirement benefits from the DCL Section of the Dow UK Pension Plan you will have the option of reducing the amount of pension you receive in exchange for a tax-free cash lump sum. The rate at which you can exchange pension for cash (commutation rate) depends on your age when you retire. For example, on retirement at the age of 60, you would currently receive £34.38 in cash (male) or £37.43 in cash (female) for each £1 of annual pension exchanged. These factors are set periodically and may change.

It is worth remembering that the pension reduction, which occurs in exchange for tax-free cash, only applies to your pension and does not reduce the amount of any spouse's pension which may be payable. Should you predecease your spouse they would still get half of the pension you would have received assuming that no tax-free cash has been taken.

In brief, each individual needs to balance the benefits of having the maximum cash upfront rather than receiving a reduced stream of income through annual pension payments. The appropriate choice will vary between individuals and will depend on personal circumstances, taking into account such things as: health, income from other sources, other assets held, as well as individual wishes and needs. The following outlines the possible advantages and disadvantages of taking a tax-free cash lump sum:

Advantages:

1) The lump sum payable is completely tax-free, whereas any pension will be subject to income tax at your highest marginal rate.

2) Any lump sum is paid up front and could be used for any specific purpose. For example: paying off the mortgage, buying a car, holiday etc.

3) The lump sum could actually be used to provide additional income, for example through a purchased life annuity. A purchased life annuity is very similar to a pension whereby any individual who is aged 55 or over can approach an insurance company and exchange a lump sum (minimum £20K) from any source for a guaranteed income for the rest of their life. Purchased life annuities have favourable tax treatment as part of the annuity is treated as a return of capital and therefore this part will be tax-free.

4) As an alternative to a purchased life annuity, the lump sum could be invested in a variety of assets. This could be used to generate an additional income or potentially generate a greater fund for the future.

5) Any unspent lump sum forms part of your estate on death and can be passed onto your beneficiaries. Your pension would stop automatically on your death (except if you die within 5- years of retirement). Any spouse's pension due would still be payable and is unaffected by giving up pension for a lump sum.

Disadvantages:

1) Taking a lump sum will reduce the amount of annual income you receive for every year for the rest of your life.

2) If the lump sum is not used for a specific purpose and ends up in a savings account then it may be more efficient to leave the money locked in the pension scheme providing additional income.

3) If a lump sum is used to provide additional income through a purchased life annuity, the annuity rates tend to be unfavourable and therefore it would be difficult to provide the same level of income compared with that which has been sacrificed in order to provide the lump sum. However, higher annuity rates may be used in the event of certain medical conditions.

It is possible to obtain a higher tax-free cash lump sum and limit the reduction in pension income by paying Additional Voluntary Contributions (AVC's). From April 2006, any AVC's paid, subject to limitations and the Trustees discretion, can be entirely used to provide cash. An alternative to providing cash is to use all or part of your accumulated AVC fund at retirement to provide additional pension, either through the DCL Section of the Dow UK Pension Plan or by buying an annuity on the open market.

Please remember that the decision to take a tax-free cash lump is a personal decision and depends on an individual's circumstances and it is always recommended that you seek appropriate financial advice on this matter