Benefits Of A Living Annuity

Upon retirement we all need peace of mind in terms of maintaining our current lifestyle, however, this calls for important decisions regarding sustaining this lifestyle post-retirement. There are several retirement products one can invest in before retirement which includes preservation funds, retirement annuities, provident and pensions. I have decided to narrow it down to living annuities, which is a post-retirement product.

Due to the need to maintain your present lifestyle, a lot of questions can be asked in reference to annuities such as: Should I invest my retirement funds into a living annuity? If I choose a living annuity, will I run out of funds before I die? If I choose a living annuity how will this benefit me? This article unfolds the benefits of investing in a living annuity.

To answer these questions, I am going to center my thoughts on the benefits and demerits of living annuities, which I believe is sustainable in the long term relative to other post-retirement products. Firstly, the most important benefit is that you are allowed to nominate a beneficiary, thereby securing the remaining capital for your spouse or heirs. This will give you surety that when you pass away your beneficiaries will have some sort of income. Since a living annuity does not form part of your estate, your beneficiaries will have immediate access to the funds. If no beneficiaries are nominated, then the funds in your living annuity will be paid into your estate.

When your beneficiaries have received the funds from your living annuity, they have three options to choose from which are:

- Option 1: Withdraw the living annuity as a lump sum;
- Option 2: Transfer the living annuity in their name and
- Option 3: Withdraw a portion as a lump sum and invest the balance into a living annuity in their name.

Please note if your beneficiaries elect to do a withdrawal, tax is charged in the hands of the deceased. If they elect to take a living annuity the income will be taxed in the hands of the beneficiary.

Another benefit as per legislation, you can draw an income from your living annuity that is levelled between 2.50% to 17.50% per year of the value in your living annuity. You can choose whether you would like to receive your income on a monthly, quarterly, bi-annually, or annually, however, this largely depends on your lifestyle bearing in mind that your income does not fluctuate if the value of your investment changes. On the anniversary date you are able to change the level of your income and this should be discussed with your financial advisor to ensure that your withdrawal does not exceed your investment growth rate.

You can determine your own asset allocation which is not restricted by Regulation 28 of the Pension Funds Act. Asset allocation deals with spreading your living annuity into different asset classes thus reducing risk concentration on one asset class. Your asset allocation should be based on your risk tolerance and return objectives, thus aiming at maintaining your income level and providing long term growth. It is often best to consult your financial advisor to help you determine the asset allocations of your living annuity.

One of the downsides of a living annuity is that the investment value and returns are not guaranteed and may increase or decrease. The value of your investment depends on the market value of the underlying investments. If there is a downfall in the markets, then your capital could reduce or not keep up with inflation. Another downside is that your income will be taxed as per the income tax table. Generally, costs are an important consideration and can be very expensive. Most living annuities charges an initial advisor fee, annual advisor fee, administration fee and investment management fee. These fees can be as high as 2.50% per annum and can accelerate the depletion of your capital.

Keeping the above benefits in mind, a living annuity may be a viable long term investment solution depending on your return objective and lifestyle goals. Regardless of market volatilities that may affect your investment, your investment strategy must be fully anchored in achieving your desired long-term financial goals.