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Understanding retirement decisions

The impact of pension lump sums and their long-term implications

New research reveals a concerning trend among those approaching retirement^[1]. One in five individuals (21%) who accessed a cash lump sum from their pension pot did so as soon as they reached 55, often without fully comprehending the potential long-term consequences. While some utilised the funds to meet immediate financial needs, others withdrew their savings simply because they could.

The findings, gathered from individuals over 50 to better understand retirement decisions and planning, provide deeper insight into this behaviour. Of those surveyed, 32% cashed their pensions to cover essential expenses. However, a larger portion – 46% – admitted they withdrew their lump sums simply because the option was available. Although these choices might appear harmless initially, the lack of proper planning often results in significant risks later on.

HIDDEN RISKS OF WITHDRAWALS WITHOUT ADVICE

The research highlights the risks linked to withdrawing pension funds without seeking professional guidance or advice. Alarming, over a quarter (27%) of adults aged 50 or older made significant decisions regarding their pensions without consulting a financial adviser or using

guidance tools. This lack of preparation often exposes them to unexpected tax liabilities or even reduced eligibility for means-tested benefits.

A notable 24% of participants admitted they were unaware that withdrawing large lump sums from their pension savings could negatively impact their eligibility for benefits. Furthermore, an additional 11% reported that accessing their savings had already directly affected their means-tested benefits. These findings highlight the critical importance of understanding the potential consequences before proceeding with pension cash-outs.

TAX-FREE ALLOWANCES OFFER SOME RELIEF

Despite the risks, some retirees aim to stay within the limits of tax-free allowances. Two-thirds (67%) of respondents who accessed their

funds withdrew 25% or less of their pension to avoid incurring taxes on the withdrawal. However, 10% opted to withdraw their entire pot, which could expose them to high tax rates or limit their financial security in later years.

If given the chance to reassess their choices, many individuals would manage matters differently. Approximately 18% admitted that, in hindsight, they would have taken out less or avoided withdrawing lump sums from their pensions. These statistics emphasise that a hasty decision during retirement planning can lead to regrets later on.

RECOGNISING THE TRUE COSTS OF EARLY ACCESS

Why do individuals opt to cash in their pension pots at such an early stage? For some, it's a matter of necessity – covering essential expenses like household bills or debts. However, the frequency of





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individuals accessing funds simply because 'they can' highlights the potential risks of not fully grasping the seriousness of these choices.

Untimely cash withdrawals can lead to numerous problems. In addition to tax penalties, they may deplete savings earlier than expected, jeopardising financial stability in future decades. Even more troubling is the possibility of losing access to critical benefits, leaving retirees without the safety nets they might rely on later.

HOW TO MAKE WELL-INFORMED DECISIONS

Individuals approaching retirement must carefully evaluate their needs and options to avoid these common pitfalls. Obtaining professional financial advice will help retirees better understand the implications of their decisions, whether they relate to taxes, benefits or ensuring long-term financial security.

Equally, adhering to this advice will provide a clear understanding of how lump sum withdrawals could affect one's financial situation in the years to come. The insights gained will enable retirees to make informed decisions tailored to their specific circumstances.

PLAN TODAY, AVOID REGRET TOMORROW

While the ability to access a pension pot at 55 offers significant flexibility, it also involves complexities that should not be overlooked. On one hand, this early access enables individuals to meet

urgent financial needs, such as settling debts, financing home improvements or even assisting loved ones.

It can also provide a sense of liberation, enabling individuals to enjoy their savings while they remain in good health and active. However, this freedom should be approached with caution. Without careful consideration, early withdrawals can significantly reduce the funds available for later years, potentially leaving retirees facing financial hardship or an uncertain future. ■

ARE YOU PREPARED TO ENSURE YOUR LONG-TERM FINANCIAL WELLBEING?

By taking the time to evaluate all options and seek expert guidance, you can make informed decisions that not only meet your current needs but also secure your long-term financial wellbeing. If you have any questions or would like personalised advice tailored to your retirement plans, please do not hesitate to contact us. Seeking guidance at this time can significantly impact your financial future.

Source data:

[1] Research conducted, on behalf of Legal & General, by Opinium between 3–9 December 2024, among 3,000 UK over 50s.

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