



Association of British Insurers

Jargon Buster: Pensions & Retirement

Introduction

This Jargon Buster defines the key terms you are most likely to encounter if you are thinking of starting a pension, already have a pension, or are thinking about retiring and how to turn your pension into a retirement income.

It is intended to provide you with an 'at a glance' understanding of key terms, and to be used in conjunction with other sources of information, rather than as a sole source of information.

The key terms and their definitions are listed in alphabetical order. Where terms are known by more than one name, the definition is provided with the term which providers use most commonly.

Key Terms

A

Annual allowance

The maximum amount that can be saved by you or on your behalf in a [pension](#) scheme each year without giving rise to a tax charge.

Annuitant

A person receiving a regular [retirement income](#) from an [annuity](#).

Annuity (also called Compulsory annuity, Lifetime annuity, or Pension annuity)

An [annuity](#) converts money from your pension fund into a regular taxable income in your [retirement](#). There are different types to suit your circumstances, but most annuities guarantee to provide you with an income until you die. Generally, you cannot change or cash in your [annuity](#).

Annuity protection – see Value protection

Annuity rate

The annuity rate determines the amount of regular [retirement income](#) you can buy with your pension fund. It is dependent on factors such as your life expectancy, expected investment returns and the type of [annuity](#) you choose. Annuity rates offered by different providers vary and are subject to regular change.

Annual Management Charge (AMC)

The Annual Management Charge (AMC) covers the costs associated with the administration, investment and distribution of a [defined contribution](#) pension plan.

B

Beneficiary

A person nominated to receive benefits under a [pension](#) scheme, or who will benefit in certain events, such as the death of the [pension](#) scheme member or [annuitant](#).

C

Capital protection – see Value protection

Commutation – see Trivial Commutation

Company pension (also called Occupational pension and Workplace pension)

A [pension](#) scheme set up by an employer. Typically both the employer and the employee make regular contributions into the scheme. Company pensions can be either [defined contribution](#) or [defined benefit](#) schemes.

Compulsory annuity – see Annuity

D

Default Fund (also called Default Investment Fund)

If you have a [defined contribution](#) pension scheme, it may offer a default fund. Your pension contributions will be invested in the default fund if you make no decision or if you choose it over the other funds available.

Defined Benefit pension scheme (also called Final Salary pension scheme)

A type of [company pension](#) where what you get when you retire depends on your [pensionable earnings](#) and years of membership of that pension scheme. Compare with [Defined contribution pension scheme](#).

Defined Contribution pension scheme (also called Money Purchase pension scheme)

A [pension](#) scheme that provides [retirement](#) benefits based on the amount of money paid in and investment growth on this money. At [retirement](#) you can shop around to choose how your regular [retirement](#) income will be provided from the scheme. All [personal pension](#) schemes, including [stakeholder schemes](#), are defined contribution [pension](#) schemes.

E

Enhanced annuity (also called Impaired annuity)

A type of [annuity](#) that may pay you a higher regular [retirement](#) income if your life expectancy is shortened because of your lifestyle (for example if you smoke) or your medical history. The [annuity](#) provider will normally ask for a medical questionnaire to be completed and a report from your doctor for this type of [annuity](#).

Escalating annuity (also called Index-linked annuity, Inflation-linked annuity and RPI- escalating annuity)

An option for your [retirement](#) income to increase in line with an inflation index, or to increase at an agreed fixed rate each year. The starting level of [retirement](#) income may be lower than for a [level annuity](#).

.....

F

Final Salary pension scheme – see Defined Benefit pension scheme

.....

G

Group Personal Pension (also called Group Personal Pension (GPP) Plan, or GPP)

A type of [personal pension](#) scheme set up by an employer on behalf of its employees. Although arranged by the employer, who can also make contributions, each [pension](#) contract is between the [pension](#) provider and the employee.

Guaranteed Annuity Rate (GAR)

A feature written into the conditions of some older [pension](#) plans. It provides a fixed rate for converting a fund into a [retirement](#) income and does not alter with changing investment conditions. A GAR is only available if you take the [annuity](#) offered by your existing pension provider. This is usually (but not always) more generous than those available on the [open market](#), but may have conditions that limit the way or the time when your [annuity](#) is paid.

Guarantee period

The [retirement](#) income from your annuity will normally stop on your death, but you can opt for your [annuity](#) to pay out for a minimum number of years, usually five or ten years, even if you die within this time. If you die before this period ends, the [annuity](#) will continue to be paid, usually to your spouse, civil partner, or to your estate, for the rest of the Guarantee period. If you live past the Guarantee period, the [annuity](#) will continue to pay you a [retirement](#) income until you die. This is different from a [joint-life annuity](#).

.....

I

Impaired annuity – see Enhanced annuity

Income drawdown (also called Income withdrawal or Unsecured pension)

This is an option available from some [defined contribution](#) pension schemes, which allows you to take an income directly from your [pension](#) fund rather than using it to buy an [annuity](#). Your [pension](#) fund remains invested and so is subject to investment risks and returns. The amount of income you can take is subject to minimum and maximum limits set by the Government and is reviewed periodically. The income you receive is taxable.

Income withdrawal – see Income drawdown

Index-linked annuity – see Escalating annuity

Inflation-linked annuity – see Escalating annuity

Inflation

This is the percentage change in the cost of living over time, measured through the Consumer Prices Index (CPI) or Retail Prices Index (RPI). As prices rise, so the value of money falls.

Investment-linked annuity

An [annuity](#) where the [retirement](#) income you receive depends on the investment returns from underlying investments in assets such as stocks and shares. This means that the amount of regular [retirement](#) income paid from the [annuity](#) can go up if the investments perform well, but can go down if the investments perform poorly. Investment-linked annuities can be either [unit-linked annuities](#) or [with-profits annuities](#).

J

Joint-life annuity

This pays you a regular [retirement](#) income for the rest of your life. On your death, it provides a regular [retirement](#) income (at the same or a reduced amount) to your surviving husband, wife, civil partner or dependant. Compare with [Single-life annuity](#).

L

Level annuity

A type of [annuity](#) that pays you the same amount of regular income from the start of your [retirement](#) until the end of any [guarantee period](#) or until your death.

Lifetime allowance

The total pension funds you can build up in your lifetime without paying extra tax. If you exceed this allowance, your pension savings may be subject to extra taxation. The lifetime allowance is reviewed and changed periodically by the Government.

Lifetime annuity – see Annuity

M

Market Value Adjustment (MVA) – see Market Value Reduction (MVR)

Market Value Reduction (MVR) (also called Market Value Adjustment (MVA))

A reduction made to the value of a [with-profits](#) fund if you cash in some or all of your with-profits investment before your [Selected Pension Age](#). Firms use MVRs to help ensure that policyholders who cash in some or all of their with-profits investment before the end of the policy term do not disadvantage the remaining policyholders.

Money Purchase pension scheme – see Defined Contribution pension scheme

N

Normal Retirement Age (NRA)

If you have a [defined benefit](#) pension scheme, this is the age at which your [pension](#) scheme specifies your [pension](#) benefits will come into payment. Compare with [Selected Pension Age](#).

O

Occupational pension – see Company pension

Open Market – see Open Market Option

Open Market Option (OMO)

Your right to shop around to compare [annuity rates](#) and different types of [annuity](#) offered by different annuity providers, and to buy an [annuity](#) from any provider you choose. The Open Market Option is only relevant for [pension](#) funds built up in [defined contribution](#) pension schemes.

P

Pension (also known as Pension fund, Pension income or Retirement income)

This term is used to refer to **either** the pot of money built up over a number of years (also known as **Pension fund**), i.e:

- a long-term investment where you can build up a pot of money from your own pension contributions, those of your employer and [tax relief](#) added to your contributions (see [Defined Contribution pension scheme](#))

and

- the [retirement](#) income you are promised from a [Defined Benefit pension scheme](#).

Or during [retirement](#), the income you are paid from this pension fund (also known as **Pension income** or **Retirement income**).

Pension annuity – see Annuity

Pensionable earnings

The earnings on which the pension benefits from a [defined benefit](#) scheme are calculated. This is usually your basic annual earnings before any bonuses, overtime and commissions. This will normally be set out in your [pension](#) documents.

Pension Commencement Lump Sum – see Tax-Free Lump Sum

Personal Pension

A type of [defined contribution](#) pension scheme into which you and/or your employer make contributions.

Phased Retirement

A way to convert part of your pension fund into an [annuity](#) or [income drawdown](#), while the rest of your [pension](#) fund remains invested. You can later use other portions of your fund to take more income. Each time you convert a portion of your fund into income, you can take some as a [tax-free lump sum](#) (normally up to 25% of the value of each portion).

Purchased life annuity

An [annuity](#) you can buy using personal funds, rather than using the funds from your pension scheme. It provides a regular [retirement](#) income in a similar way to a [lifetime annuity](#), although the taxation rules differ.

R

Retirement income – see Pension

Retirement

For the purposes of pensions, retirement is when you take income from your [pension](#) fund. Retirement does not necessarily mean you have given up work.

RPI-escalating annuity – see Escalating annuity

S

Selected Pension Age

When you start a [personal pension](#) plan, you choose an age at which you expect to start taking a [retirement](#) income. Compare with [Normal Retirement Age](#).

Single-life annuity

If you choose this type of [annuity](#), the [retirement](#) income paid stops on your death or at the end of the [guarantee period](#), if you have one, whichever is later. Compare with [joint-life annuity](#).

SIPP (Self-Invested Personal Pension)

A type of [personal pension](#) plan that allows you to choose to invest your [pension](#) contributions from a wider range of investment options than other types of [personal pension plan](#).

Stakeholder Pension

A type of [personal pension](#) that has to meet certain standards set by the Government.

Statutory Money Purchase Illustration (SMPI)

A forecast of the amount of [retirement](#) income your pension pot may be able to buy when you retire, based on assumptions set out by regulations. This is shown in the annual [pension](#) statements issued by providers to members of [defined contribution](#) pension schemes.

T

Tax-free cash – see Tax-free lump sum

Tax-free lump sum (also called Pension Commencement Lump Sum (PCLS) and Tax-free cash)

A one-off amount of cash up to a maximum set by the Government, that you can take free of tax from your [pension](#) fund when you decide to draw retirement benefits. Some [pension](#) arrangements may have specific rules on how much you can take.

Tax relief

Tax relief means you do not pay any Income Tax on the contributions you and/or your employer make into your [pension](#) scheme. Funds held in the scheme also receive favourable tax treatment. Income tax is payable on any income taken from the scheme.

Trivial commutation (also called Commutation and Trivial payment)

If the total of all your [pension](#) savings (excluding state pensions) at [retirement](#) are below a certain limit set by the Government, you may be able to withdraw your entire savings from your [pension](#) fund(s) as a cash lump sum, part of which is taxable.

Trivial payment – see Trivial commutation

U

Unit-linked annuity

A type of [investment-linked annuity](#) where the [retirement](#) income paid to you is linked to the performance of units in investment funds. The [retirement](#) income therefore varies and may go up or down.

Unsecured pension – see Income drawdown

V

Value protection (also called Annuity protection or Capital protection)

If you take out an [annuity](#), you can choose to add this option. It means that when you die, a [beneficiary](#) you've nominated will be paid a lump sum or a chosen percentage of the value of your [pension](#) fund when you set the [annuity](#) up less the [annuity](#) income you took from it while you were alive. The payment is subject to a tax charge.

W

With-profits annuity

A type of [investment-linked annuity](#) where the [retirement](#) income paid to you is linked to the performance of the [annuity](#) provider's with-profits fund. The [retirement](#) income you will receive each year may go up or down.

Workplace pension – see Company pension