HM Revenue & Customs

Pensions Flexibility: Draft guidance on clauses for the Taxation of Pensions Bill

Draft Guidance
5 August 2014

Contents

Introduction

At Budget 2014, the Government announced the most fundamental change to how people can access their pension savings in nearly a century. From April next year, individuals with money purchase savings will be able to access their entire pension fund flexibly if they wish. This will allow individuals to make their own choices about how to use their pension savings.

To allow for this new flexibility, a number of changes need to be made to the existing pensions tax legislation in Finance Act 2004. These changes will be made in a Taxation of Pensions Bill which will be introduced in the autumn.

In August 2014, HMRC published for consultation most of the draft clauses that are intended to be included in the Taxation of Pensions Bill. This draft guidance is intended to support these draft clauses. It does not cover any legislative changes that will be in the DWP Pension Schemes Bill such as the Guidance Guarantee or the regulatory framework for defined ambition pension schemes. It is also not intended to provide detail on the existing pensions tax legislation. Guidance on this can be found on the HMRC website and in the Registered Pension Schemes Manual.

If you have any questions or comments in connection with this draft guidance or the draft legislation, please send them to pensions.policy@hmrc.gsi.gov.uk by close on 3 September 2014. Alternatively you can phone 03000 564209, 03000 564149 or 03000 564289.

Chapter 1 Background

What do the published clauses cover?

From April 2015, changes are being made to pension tax rules to give individuals aged 55 and over greater flexibility to access their pension savings. The changes in the published draft clauses will;

- remove the higher tax charges where people take pensions under money purchase pension savings as they wish;
- increase the flexibility of the income drawdown rules by removing the maximum 'cap' on withdrawal and minimum income requirements for all new drawdown funds from 6 April 2015;
- enable those with 'capped' drawdown to convert to a new drawdown fund once arranged with their scheme
- enable pension schemes to make payments directly from pension savings with 25 per cent taken tax-free (instead of a tax-free lump sum)
- introduce a limited right for scheme trustees and managers to override their scheme's rules to pay flexible pensions from money purchase pension savings
- remove restrictions on lifetime annuity payments;
- ensure that individuals do not exploit the new system to gain unintended tax advantages by introducing a reduced annual allowance for money purchase savings where the individual has flexibly accessed their savings; and,
- increase the maximum value and scope of trivial commutation lump sum death benefits.

How do the changes work

From 6 April 2015, you will be able to take as little or as much as you want (known as crystallisation) from a money purchase arrangement once you have reached normal minimum pension age (normally age 55). You will have the choice of taking your funds as an income for life, for example by purchasing a lifetime annuity, or you can access as much of your funds when you want. Or you can do both.

To access your funds you will have two main choices;

- you can put your funds into a drawdown fund, known as a flexi-access drawdown fund from which you can drawdown any amount over whatever period you choose; or
- you can take a single or series of lump sums from your uncrystallised funds, (known as an uncrystallised funds pension lump sum.

The amount of tax due will depend on how you take your pension funds (and on your own personal circumstances). See Tax on workplace, personal or foreign pensions

Any payments from a flexi-access drawdown fund will be taxable as a pension, however you can have a tax free lump sum of up to 25% of your pension fund when you put funds into a flexi-access drawdown fund.

Any payment of an uncrystallised funds pension lump sum will be 25% tax free, with the remainder taxable as if it were a pension.

See Chapter 2 of this guidance note for more information about your choices.

From 6 April 2015 certain flexible access payments on or after 6 April 2015 will trigger the money purchase annual allowance rules. This will limit the amount of tax relief you can get on future savings to any money purchase arrangement. See Chapter 3 of this guidance note.

The changes will also ensure that if you have already taken (or 'crystallised') your pension from a money purchase arrangement, the current tax rules can continue to apply to any payments of pension that you receive on or after 6 April 2015 and you will not trigger the Money Purchase Annual Allowance rules unless or until you take benefits under the new rules.

Even if on 5 April 2015 you have an existing drawdown pension fund, then you will still be able to take advantage of the new flexibilities if you wish. Receiving certain payments under the new rules will mean however that you will trigger the money purchase annual allowance rules. See Chapter 5 of this guidance note.

When will the Taxation of Pensions Bill be introduced?

The Bill will be introduced into Parliament in autumn 2014.

What benefits can I take from a money purchase arrangement from April 2015?

When you come to take your benefits from a money purchase arrangement under a registered pension scheme on or after 6 April 2015 from age 55, you will be able to choose one or more of the following options:

- Buying a lifetime annuity - see RPSM09101700,
- Designating some or all of your fund to provide a drawdown pension - see RPSM09103500,
- Taking an uncrystallised funds pension lump sum - see below,
- Taking a scheme pension - see RPSM09101200

Lifetime annuity and drawdown pension

If you buy an annuity or designate funds as available for drawdown you will, as now, also be able to receive at the same time, a tax-free lump sum, (known as a 'pension commencement lump sum' or 'PCLS'). The maximum amount of this lump sum is an amount equal to one third of the value of your annuity or of the funds that you have designated for drawdown. Any other money paid to you from the annuity or the drawdown pension will be taxable as pension income.

If you flexibly access your drawdown pension on or after 6 April 2015, the tax relief on any further pension savings you make to a money purchase arrangement will be restricted. You will receive tax relief only on money purchase pension savings up to £10,000 a year. Any excess will not benefit from tax relief as you will be liable to the annual allowance charge on the excess. See chapter 3 of this guidance.

Uncrystallised funds pension lump sum

If you take an uncrystallised funds pension lump sum, one quarter of the amount paid will normally be tax-free, the remainder will be taxable as pension income.

If you take an uncrystallised funds pension lump sum, the tax relief on any further pension savings you make to a money purchase arrangement will be restricted. You will receive tax relief only on money purchase pension savings up to £10,000 a year. Any excess will not benefit from tax relief as you will be liable to the annual allowance charge on the excess. See chapter 3 of this guidance.

Scheme pension

If you take a scheme pension, the maximum tax-free lump sum is calculated as an amount equal to one third of the value of the sums and assets in your fund that are taken to provide the scheme pension.

There may also be circumstances when you can take your pension savings as a small pot lump sum. See Options when you take your pension

What is a money purchase arrangement?

A money purchase arrangement can be in the form of either a cash balance arrangement or a defined contribution arrangement (known as an 'other money purchase arrangement'). See Types of pension schemes for further information on money purchase arrangements.

What is a lifetime annuity?

From 6 April 2015, to be a lifetime annuity, the annuity must be payable at least annually to the member by an insurance company and must be payable at least until the member's death. Payments from a lifetime annuity are taxed as income of the recipient.

From 6 April 2015, some of the current restrictions on a lifetime annuity will be removed.

- The annual rate of the lifetime annuity will be allowed to go down as well as up.
- There will no longer be a requirement that the member must have been given the opportunity to select the insurance company, although schemes may still offer the member this opportunity should they wish.
- The current 10-year restriction on the period for paying the income from a lifetime annuity after the member's death will be removed. A lifetime annuity may continue to be paid after the member's death for any period that is set out in the annuity contract.

Example 1

Elaine, aged 65, has pension savings in her defined contribution scheme of £200,000. In May 2015 she decides she wants to buy a lifetime annuity. She can have £50,000 paid to her as tax-free lump sum. The remaining £150,000 is paid to an insurance company to provide her with an income. Initially she receives £7,000 a year. This counts as taxable pension income and Elaine is therefore liable to any income tax due on it, although if she has no other income, the total paid will be within her personal allowance and no tax will be payable.

What is a drawdown pension?

A drawdown pension can take different forms;-

- a short-term annuity paid to you by an insurance company; or,
- a pension paid to you from someone other than an insurance company (known as income withdrawal). The payments do not have to be regular and can vary.

See Options when you take your pension for further information on taking a drawdown pension before 6 April 2015.

What are the options for a drawdown pension from 6 April 2015?

From 6 April 2015 a new drawdown pension can be either;

- Income withdrawal – where you can take how much you want, when you want; or,
- A short-term annuity – where all or some of your drawdown funds are passed to an insurance company to buy an annuity that will pay an income to you for up to 5 years.

However depending on whether the drawdown fund already existed on 5 April 2015 (a drawdown pension fund) or is a new drawdown fund set up on or after 6 April 2015 there are slightly different rules

What if I already have a drawdown pension on 5 April 2015?

If you have designated funds as available for drawdown prior to 6 April 2015 your drawdown pension may be either
Capped drawdown - see RPSM09103530, or
Flexible drawdown - see RPSM09103590

The options available to you depend on the form of your current drawdown pension and whether or not you are designating funds under the same arrangement.

Whichever option you choose when you designate the new funds as available for drawdown, you will be able to receive at the same time a tax-free lump sum (a pension commencement lump sum) of an amount up to one third of the value of the newly designated funds.

If you designate funds under an arrangement that before 6 April 2015 didn't contain a drawdown pension fund the funds will be designated into what is known as a flexi-access drawdown fund. There will be no limit on the amount that you can draw from the fund each year. You will be able to take payments whenever you like, for example as a regular stream, or just as one or more lump sums. Any payment from the flexi-access drawdown

fund will be taxable as pension income and will trigger the money purchase annual allowance rules.

If before 6 April 2015 you were taking your pension as flexible drawdown, your drawdown pension fund will convert automatically to a flexi-access drawdown fund on 6 April 2015. The money purchase annual allowance rules will apply to you from that date. Any further designations under the arrangement holding the drawdown fund will go into the converted flexi-access drawdown fund.

If on 5 April 2015 your existing drawdown fund was paying a capped drawdown pension and you designate new funds under the same arrangement that holds the capped drawdown fund you have two options.

1. Before you designate the funds you can convert your capped drawdown pension fund into a flexi-access drawdown fund. If you do this the newly designated funds will be designated to the converted flexi-access drawdown fund. When you access any of these funds this will trigger the money purchase annual allowance rules.
2. You do not convert your existing capped drawdown pension fund into a flexi-access drawdown fund. Your newly designated funds will be designated to your existing capped drawdown pension fund. The limit on the maximum amount of pension you can draw each year will continue to apply to that fund (including all the administration needed to review and calculate that maximum amount).

However as long as

- the drawdown pension you get is not more than your maximum capped drawdown amount, or
- you have not flexibly accessed you pension funds under another arrangement or as an uncrystallised funds pension lump sum,

then the money purchase annual allowance rules won't apply to you.

I have not had a drawdown pension fund before 6 April 2015

To qualify for a drawdown pension you must first designate funds as available for drawdown with your pension provider. If you do not have an existing drawdown pension fund on 5 April 2015, you must designate those funds to a new drawdown fund, known as your flexi-access drawdown fund.

When you designate the new funds as available for drawdown, you will be able to receive at the same time a tax-free lump sum of an amount equal to one third of the value of the funds you have put into your flexi-access drawdown fund.

If you designate funds as available for drawdown to a flexi-access drawdown fund, and subsequently access any of those funds, whether in the form of income withdrawal or a short term annuity, then you will be subject to the money purchase annual allowance rules and you will receive tax relief only on money purchase pension savings up to £10,000 a year. See Chapter 3 of this guidance.

How can I take my drawdown funds?

Once you have designated funds into a drawdown fund, there are two ways you can access them, income withdrawal or a short term annuity.

What is income withdrawal?

If you choose income withdrawal from your flexi-access drawdown fund, you can then take as much or as little as you like each year from this regardless of any other income you may have.

If you choose income withdrawal from your or pre-6 April 2015 drawdown pension fund, you can if you wish continue to take no more than the current annual maximum for capped drawdown. However whereas before 6 April 2015 if you take more than the cap, the excess payment over the cap is an unauthorised payment, from 6 April 2015 an excess payment over the annual cap will not be an unauthorised payment, but the capped drawdown fund will automatically be converted to a flexi-access drawdown fund.

You are liable to income tax on whatever you take out from your flexi-access drawdown fund or pre-6 April 2015 drawdown pension fund.

Example 2

Dinta has £40,000 in a money purchase arrangement which she wants to take benefits from through drawdown. She hasn't previously designated any funds to a drawdown pension fund.

Dinta therefore designates £30,000 to a flexi-access drawdown fund. At the same time, she receives from her money purchase arrangement a tax-free lump sum of £10,000 (one third of the value of the funds she put into drawdown).

Dinta does not have to take any money from her flexi-access drawdown fund, but when she does she will trigger the money purchase annual allowance rules.

Example 3

John has £50,000 in a money purchase arrangement which he wants to take benefits from through drawdown. He has prior to 6 April 2015 designated funds to a drawdown pension fund which he is taking as capped drawdown. John has the choice of designating the additional funds to a new flexi-access drawdown fund, to his existing drawdown pension fund or converting his existing fund into a flexi-access drawdown fund and then designating into that converted flexi-access drawdown fund.

John decides he wants to continue with his existing capped drawdown pension fund and therefore designates £37,500 to the drawdown pension fund. At the same time, he receives

from his money purchase arrangement, a tax-free lump sum of £12,500 (one third of the value of the funds he put into drawdown).

As long as John does not receive payments in excess of the capped drawdown limit from his drawdown fund, he will not trigger the money purchase annual allowance rules.

Example 4

Tom, aged 58, has pension savings in his money purchase scheme of £120,000. He has no other pension savings but is still employed and receives an income of £27,000 a year. In December 2015, he decides that he wants to put the funds into a flexi-access drawdown fund. He can have £30,000 paid to him as a tax-free lump sum. The remaining £90,000 is designated as available for drawdown.

In the first year Tom takes £5,000 from his flexi-access drawdown fund. His total taxable income for the year is therefore £32,000. As this is less than the higher rate threshold, Tom is liable to income tax at basic rate on all his income.

In the second year Tom takes £25,000 from his flexi-access drawdown fund. His total taxable income for the year is therefore £52,000 and he will be liable for income tax at higher rate on the amount over the higher rate threshold, and at basic rate on the amount between his personal allowance and the higher rate threshold.

What is a short-term annuity?

From 6 April 2015, if you choose to buy a short-term annuity with some or all of the funds in your flexi-access drawdown fund or existing capped drawdown pension fund, the annuity must be payable at least annually to you by an insurance company and must be payable for no more than 5 years.

From 6 April 2015, the income you receive from a short-term annuity may go down as well as up, and there will no longer be a requirement that you must have been given the opportunity to select the insurance company, although schemes may still offer you this opportunity should they wish.

What is an uncrystallised funds pension lump sum?

From 6 April 2015, if you want to access some or all of your money purchase pension savings without first designating funds as available for drawdown, you can have an uncrystallised funds pension lump sum.

Normally one quarter (25 per cent) of the amount paid will be tax-free, with the remainder taxable as pension income. You can not also have a pension commencement lump sum in connection with an uncrystallised funds pension lump sum.

To qualify as an uncrystallised funds pension lump sum

- It must be payable from uncrystallised rights held under a money purchase arrangement
- You must have more lifetime allowance remaining than the amount of the lump sum if you are under age 75 when it is paid
- If you are 75 or over when the lump sum is paid, you must have at least some lifetime allowance remaining at that time, and
- You must have reached age normal minimum pension age (55) or meet the ill-health conditions.

An uncrystallised funds pension lump sum cannot be paid from a drawdown fund.

You also cannot be paid an uncrystallised fund pension lump sum if immediately before the lump sum is paid;

- You have either primary protection and/or enhanced protection with protection of lump sum rights of more than £375,000 (see RPSM03105135 and RPSM03105185); or,
- You have a lifetime allowance enhancement factor (due to primary protection, pension credits from previously crystallised rights, non-residence, transfers from recognised overseas pension schemes or pre-commencement pension credits) and the available portion of your lump sum allowance is less than 25 per cent of the proposed uncrystallised funds pension lump sum.

This provision ensures that you cannot get an uncrystallised funds pension lump sum that would give you a bigger tax-free amount than you could be paid as a tax-free pension commencement lump sum.

If you take an uncrystallised funds pension lump sum on or after 6 April 2015, you will be subject to the money purchase annual allowance rules from that date. Any excess money purchase pension savings will not benefit from tax relief you will be liable to the annual allowance charge. See Chapter 3 of this guidance.

Example 5

Naresh, aged 61, is currently a higher rate tax payer with an income of £70,000 per annum. He has pension savings in a money purchase arrangement of £340,000. In October 2015, Naresh decides not to designate funds as available for drawdown but instead takes a one-off payment of £120,000 from his pension scheme which qualifies as an uncrystallised funds pension lump sum.

Naresh can receive 25% of this payment tax-free (£30,000) and the remaining 75% (£90,000) is taxed as pension income.

His total income for the year is therefore £160,000 and as this is greater than the additional rate threshold of £150,000, £10,000 of his income will be taxed at the additional

rate of 45%, with the remaining income in excess of his personal allowance taxable at basic or higher rate.

If you are under age 75 when your uncrystallised funds pension lump sum is paid, the full amount of the lump sum is tested against your remaining LTA as a benefit crystallisation event 6 (BCE6). A BCE6 occurs where an individual becomes entitled to certain specified lump sums. Entitlement to an uncrystallised funds pension lump sum arises immediately before it is paid. The amount of a BCE6 is the amount of the lump sum paid. When you are under 75 you can receive an uncrystallised funds pension lump sum only where at the time it is paid you have more lifetime allowance remaining than the amount of the lump sum. Any lump sum paid in excess of the individual's remaining lifetime allowance will not be an uncrystallised funds lump sum, but will be a lifetime allowance excess lump sum. See Understanding the lifetime allowance for pension schemes.

Example 6

In April 2015 Liz, aged 65, has remaining lifetime allowance of £300,000. She also has £400,000 in a money purchase arrangement which she wants to take now.

Liz can choose to take an uncrystallised funds pension lump sum of £300,000, which will use up all her remaining lifetime allowance. £75,000 of this will be paid tax-free and £225,000 will be subject to income tax. Liz can receive her remaining £100,000 as a lifetime allowance excess lump sum, which will be taxable at 55%.

If you are aged 75 or over when the lump sum is paid, you must have at least some remaining lifetime allowance remaining at that time, otherwise the lump sum is not an uncrystallised funds pension lump sum. If your lump sum is fully within your remaining lifetime allowance, you receive 25% of the lump sum tax-free and the remainder is taxable as pension income. But if the amount of the lump sum is more than your remaining lifetime allowance, there is a restriction on the amount that you can take tax-free. The tax-free part of the lump sum will be an amount equal to 25% of the amount of lifetime allowance remaining. The rest of the lump sum is taxable as pension income.

Example 7

Marmaduke is 80 years old and wants to take all the remaining funds out of his money purchase pension scheme. His previous pension statements show that he has already used up a total of 90% of his lifetime allowance which is the standard lifetime allowance and for the purposes of this example is £1.25 million at the time the lump sum is paid.

Marmaduke therefore has 10% of his lifetime allowance remaining, or £125,000. But the amount he wants to take is £150,000. The amount he can receive free of tax is therefore £31,250 (25% of £125,000). The remaining £ 118,750 is taxable as pension income.

What happens if I only have a final salary (defined benefit) pension?

You can not receive a lifetime annuity, a drawdown pension of any kind or an uncrystallised funds pension lump sum from a defined benefit arrangement.

Will there be any changes to trivial commutation lump sums/small pot lump sums?

The main change to the small pots rules is that from 6 April 2015 this type of lump sum may be paid to an individual from their normal minimum pension age (55), not age 60 as at present.

From 6 April 2015, you will not be able to receive a trivial commutation lump sum from a money purchase arrangement. The introduction of the uncrystallised funds pension lump sum provides a way to withdraw all of the funds from a money purchase arrangement from 6 April 2015.

From 6 April 2015 you will still be able to take a trivial commutation lump sum from a defined benefits arrangement and you will be able to receive such a lump sum from normal minimum pension age (55), not age 60 as at present.

See Taking a small pension pot as a lump sum.

My scheme rules don't allow me to receive all of these new payments

The legislation will include a scheme rules override. This will allow scheme trustees or managers to make payments within these new rules should they wish without having to change the scheme rules. However scheme trustees or managers will not have to make these payments if they choose not to do so. In such a case, you may wish to consider whether to transfer to another money purchase arrangement that offers the flexibility you want to opt for.

What about death benefits?

On the death of a member, death benefits can be paid as a dependants' pension and/or as a death benefit lump sum.

What are the changes to dependants' pensions?

From 6 April 2015, similar changes to the rules for dependant's annuities and dependants' drawdown pensions are being made to those for a lifetime annuity, and a member's drawdown pension.

Dependants' annuities

For annuities purchased on or after 6 April 2015 there will no longer be a requirement that;

- the member or the dependant must have been given the option to choose the insurance company providing the annuity;
- the annual rate of the annuity cannot go down; the annual rate of a dependant's annuity will be able to go down as well as up.

Dependants' drawdown pensions

Dependants will have the same options as members for drawdown pensions, as follows;

- Designations after 5 April 2015 under an arrangement where there is no pre April 2015 dependants' drawdown pension fund will be to a dependants' flex-access drawdown fund;
- Existing dependants' drawdown pension funds paying flexible dependants' drawdown pension will convert to a dependants' flexi-access drawdown fund on 6 April. Any designations to that pre-existing drawdown pension fund will be into the converted dependants' flexi-access drawdown fund;.
- Dependants may convert existing dependants' drawdown pension funds paying capped dependants' drawdown pension into dependants' flexi-access drawdown fund in a similar way to members. That is they either notify their scheme administrator they intend to convert the fund or take dependants' drawdown pension of more than the annual maximum amount for capped drawdown. Any designations to the fund after it has converted will be to a dependants' flexi-access drawdown fund;
- Dependants can choose not to convert their existing capped dependants' drawdown pension funds. Any further designations under the arrangement will be to the existing capped dependants' drawdown pension fund. The cap on the maximum amount of dependants" drawdown pension that can be paid will continue to apply. Scheme administrators will still need to carry out regular reviews and calculations of the maximum annual amount in line with the existing requirements.

However there is one significant difference between members' drawdown and dependants' drawdown. Payment from a dependant's flexi-access drawdown fund on its own will not trigger application of the money purchase annual allowance rules. Only if the individual has also received an uncrystallised funds pension lump sum or is also receiving member's flexi-access drawdown benefits will the money purchase annual allowance rules apply.

What are the changes to lump sum death benefits?

Where funds have been designated as available for drawdown on or after 6 April 2015 to a flexi-access drawdown fund, any unused funds on the death of the member can be paid as a flexi-access drawdown fund lump sum death benefit.

Any unused funds on the death of the member on or after 6 April 2015 from a pre-6 April 2015 capped drawdown pension fund that has not converted to a flexi-access drawdown fund can be paid as a drawdown pension fund lump sum death benefit as at present.

The conditions for the payment and the taxation of a flexi-access drawdown fund lump sum death benefit are the same as for the payment of a drawdown pension fund lump sum death benefit. See RPSM10106060 for further information on drawdown pension fund lump sum death benefits.

As with a drawdown pension fund lump sum death benefit, a flexi-access drawdown fund lump sum death benefit can be paid to anyone, and the maximum that can be paid is the value of the flexi-access drawdown fund at the time the lump sum is paid.

Some changes have been made to the conditions for paying a trivial commutation lump sum death benefit - see chapter 6 of this guidance.

Can an uncrystallised funds pension lump sum be paid on the death of a member to another person?

No, an uncrystallised funds pension lump sum can be paid only to the member.

Chapter 3 The money purchase annual allowance rules

The money purchase annual allowance rules have been introduced to ensure that individuals do not use the new flexibilities, which are intended to provide people with greater access to their retirement savings, to avoid tax on their current earnings by diverting their salary into their pension with tax relief, and then immediately withdrawing 25% tax-free.

What are the money purchase annual allowance rules?

If you trigger the money purchase annual allowance rules, then you will have a £10,000 annual allowance for money purchase pension savings. Depending on whether or not you exceed this £10,000, you will either have a reduced £30,000 annual allowance or you will retain the normal £40,000 annual allowance.

If you trigger the money purchase annual allowance rules and exceed the £10,000 money purchase annual allowance in any tax year,

- you will be subject to the annual allowance charge on the excess over £10,000, (see RPSM06105020), and
- your annual allowance for the remainder of your pension savings will be reduced to £30,000 (the 'alternative annual allowance') plus any unused annual allowance you may carry forward from the three previous tax years. To ensure that the same savings are not subject to the annual allowance twice, any pension savings tested against the £10,000 money purchase annual allowance will not be tested against your reduced £30,000 annual allowance.

If you do not exceed the £10,000 money purchase annual allowance,

- your total annual allowance, including for money purchase and defined benefit arrangements, will continue to be £40,000 plus any unused annual allowance carried forward from the three previous tax years,
- you will not be able to carry forward any unused money purchase annual allowance.

What are the trigger events?

The money purchase annual allowance rules will apply to you if one of the following occurs in a tax year, on or after 6 April 2015;

- you drawdown funds from a flexi-access drawdown fund, including receiving payments from a short-term annuity provided from a flexi-access drawdown fund;
- you receive an uncrystallised funds pension lump sum;

- you notify your scheme administrator that you wish to convert your pre-6 April 2015 drawdown pension fund to a flexi-access drawdown fund and you subsequently take a drawdown pension from that fund;
- you take more than the permitted maximum for capped drawdown from a pre-6 April 2015 drawdown pension fund; or,
- you receive a stand-alone lump sum and you are not entitled to enhanced protection.

In addition you will be subject to the money purchase annual allowance rules from 6 April 2015 if

- you have received prior to 6 April 2015 a flexible drawdown payment from a pre-6 April 2015 drawdown pension fund.

Example 8

David is a member of a money purchase arrangement and a defined benefit arrangement and has flexibly accessed his money purchase arrangement in the tax year. David's total savings to his money purchase arrangement for the tax year are £6,000. As this amount is not more than £10,000 there is no test against the money purchase annual allowance for the tax year concerned.

His total pension savings are therefore tested against the £40,000 annual allowance. David's total defined benefit pension savings are £32,000. This means his total pension savings for the tax year are £38,000. As this is less than £40,000, no annual allowance charge is due, and he has £2,000 unused annual allowance to carry forward to the next year.

Assuming David had no other annual allowance to carry forward from other years, the next year he will have an overall annual allowance of £42,000 but his money purchase annual allowance remains £10,000.

Example 9

Isobel is a member of a money purchase arrangement and a defined benefit arrangement and has flexibly accessed her money purchase arrangement in the tax year. She has no available carry forward. Isobel's total defined benefit pension savings for the tax year are £28,000 and her total savings to her money purchase arrangement are £11,000. As this is more than £10,000, her tax relief for the money purchase pension savings may be restricted by the money purchase annual allowance.

Isobel must now work out whether she is liable for an annual allowance charge on a chargeable amount.

In this example, it is easy to see that as Isobel's money purchase pension savings have exceeded £10,000 she is liable to an annual allowance charge on the excess of £1,000. However as her remaining defined benefits savings are less than £30,000, no annual

allowance charge arises in respect of these. Isobel is therefore liable to an annual allowance charge on £1,000 (her chargeable amount).

The legislation however sets this out in a number of steps which are as follows;

The chargeable amount is the higher of

- *the default chargeable amount which is the excess of Isobel's defined benefit pension savings plus money purchase pension savings over the annual allowance (£40,000), and*
- *the alternative chargeable amount which is the total of the excess of Isobel's defined benefit pension savings over the alternative annual allowance (£30,000) plus the excess of money purchase savings over the money purchase annual allowance (£10,000)*

That is

- *The excess of £28,000 + £11,000 over £40,000 = £0 (the default chargeable amount) or,*
- *£11,000 - £10,000 = £1,000 plus the excess of £28,000 over £30,000 (nil) = £1,000 (the alternative chargeable amount)*

In Isobel's case, the alternative chargeable amount is more than the default chargeable amount so the alternative chargeable amount applies.

Isobel will therefore be liable to an annual allowance charge on her chargeable amount of £1,000.

See Understanding the annual allowance for pension schemes for further information on the current annual allowance rules.

What payments don't trigger the Money Purchase Annual Allowance rules?

The Money Purchase Annual Allowance rules will not apply if one of the following occurs;

- You receive a tax free lump sum (a pension commencement lump sum);
- you receive a trivial commutation lump sum;
- you receive a small pots lump sum;
- you are in receipt of a scheme pension;
- you are in receipt of a lifetime annuity; or,
- After 6 April 2015, you take no more than the permitted maximum for capped drawdown from a pre-6 April 2015 drawdown pension fund.

Example 10

Karen has a small money purchase pension pot of £8,000 in one scheme which she wants to access as a lump sum.

As her savings in that scheme are less than £10,000 she can take the whole amount as a small pots lump sum, providing she has not received three such lump sums before. This can be paid 25% tax free with the remainder of £6,000 taxable as income. Taking a small pot lump sum would not trigger the money purchase annual allowance rules.

If Karen has previously had three small pot lump sums from money purchase arrangements then she could not receive a further small pot lump sum. Karen can still take the £8,000 as an uncrystallised funds pension lump sum, which will also be 25% tax free and 75% taxable as income. However the payment of an uncrystallised funds lump sum will trigger the money purchase annual allowance rules. Karen's money purchase pension savings may be subject to the money purchase annual allowance if she saves more than £10,000 into money purchase arrangements in a year and her alternative chargeable amount is more than her default chargeable amount.

So how do the rules work in the tax year the trigger event occurs?

If you have a trigger event in a tax year then you become subject to the money purchase annual allowance rules from the day after the trigger event occurred. The amount of any annual allowance charge due will depend on whether your total money purchase pension savings exceed £10,000, and whether in addition your alternative chargeable amount is more than your default chargeable amount.

For the purpose of the annual allowance generally, pension savings in a particular arrangement count for the pension input period for that arrangement that ends in a particular tax year. Each successive pension input period must end in consecutive tax years, but pension input periods do not have to match tax years. See Understanding the annual allowance for pension schemes for more information on pension input periods.

So when a trigger event occurs in a tax year there are a number of possible situations for pension input periods that may be affected

1. There may have been a pension input period that has already ended in the tax year. For example a pension input period runs from 1 October 2015 to 30 September 2016 and a trigger event occurs on 1 November 2016.
2. There may be a pension input period that will end in the tax year but hasn't ended when the trigger event occurs. For example a pension input period runs from 1 January 2015 to 31 December 2015 and a trigger event occurs on 1 December 2015.
3. There may be a pension input period ending in the next tax year, for example a trigger event occurs on 1 March 2016 where the pension input period runs 1 January to December.

In the first year that the money purchase annual allowance rules apply to you, any money purchase savings that you have made prior to triggering the rules will not be subject to the money purchase annual allowance.

So where the first situation arises then for the purposes of the £10,000 money purchase annual allowance the pension input amount for a money purchase arrangement is treated as nil. However any pension input amount for this arrangement is tested against the full annual allowance, even if other money purchase savings would have exceeded the money purchase annual allowance.

Where the second or third situation arises, the pension input amount is split into two, the amount that arose up to and including the date of the trigger event, and the amount that arose after the trigger event. Only the latter that is tested against the money purchase annual allowance. The way that the pension input amount is split depends on the type of arrangement –

- Where the money purchase arrangement is a defined contribution arrangement this split is based on the contributions for each period.
- If the arrangement is a cash balance arrangement, then the pension input amount for the arrangement is split proportionally so that if the pension input period is 365 days and the trigger event occurred 100 days before the end of the pension input period, then the pension input amount that is tested against the money purchase annual allowance is 100/365 times that pension input amount.

Example 11

On 1 November 2015, Bruce took a payment from his flexi-access drawdown fund. This triggers the money purchase annual allowance rules.

Bruce has two money purchase arrangements, the first has a pension input period of 1 October to 30 September and the second from 1 January to 31 December. Bruce contributes £400 per month to the first arrangement and £600 per month to the second arrangement.

As the pension input period for the first arrangement ends before the trigger event, the 12 contributions of £400 that are tested against the 2015-16 annual allowance are not tested against the money purchase annual allowance.

As the pension input period for the second arrangement ends after the trigger event, the contributions of two contributions of £600 paid in November and December are tested against the money purchase annual allowance.

If Bruce has no other savings, his money purchase input amount that is tested against the £10,000 money purchase annual allowance is £1,200. As this is less than £10,000, all his savings are tested against the £40,000 annual allowance for 2015-16. As these savings total £12,000, these are less than £40,000 and Bruce does not have to pay any annual allowance charge.

Note that if Bruce had started a new money purchase arrangement after 1 November 2015 but before 5 April 2015, the pension input period for that arrangement would normally end on 5 April 2015 and contributions to that arrangement would count for the total money purchase input for 2015-16, unless a later end date was nominated for the pension input period.

Example 12

Wayne triggers the money purchase annual allowance rules on 15 September 2015. He has two arrangements, a cash balance arrangement and an other money purchase arrangement.

The pension input periods for the arrangements are for twelve months and end on 31 March 2016 and 15 February 2016 respectively.

Wayne's pension input amount for his cash balance arrangement for the pension input period ending 31 March 2015 is £12,000. Wayne also makes two payments to his other money purchase arrangement of £15,000 on 1 July 2015 and £8,000 on 1 February 2015.

For the purposes of his 2015-16 money purchase annual allowance, his pension input amount is for the cash balance arrangement, £12,000 x 153 (the number of days from 16 September 2015 (the day after flexible access) to 15 February 2016 divided by 365 (days in the pension input period) = £5,030.

For the purposes of his 2015-16 money purchase annual allowance, his pension input amount is for the other money purchase arrangement is the contributions on or after 16 September 2015, that is £8,000.

Wayne's total money purchase input amount for 2015-16 is therefore £13,030. As this exceeds £10,000 he now has to work out whether his alternative chargeable amount is more than his default chargeable amount.

In Wayne's case, he has no defined benefit inputs so his alternative chargeable amount is the excess money purchase input of £3,030.

The default chargeable amount is the excess of the total pension input amount calculated under the normal rules over £40,000 (the normal annual allowance for the year).

This gives a figure of £35,000. This is within the normal annual allowance of £40,000, so the default chargeable amount is nil.

So in Wayne's case his alternative chargeable amount is higher than his default chargeable amount and the annual allowance charge will be applied to his alternative chargeable amount of £3,030.

Individuals who have received a flexible drawdown payment before 6 April 2015

If you receive a flexible drawdown payment before 6 April 2015, then under the pre-6 April 2015 (current) rules you effectively have a nil annual allowance for all types of pension savings (both money purchase and defined benefit).

On 6 April 2015, your fund will automatically become a flexi-access drawdown fund and you will be subject to the money purchase annual allowance rules from that date. However your annual allowance will be the same as anyone else who has triggered the money purchase annual allowance rules. Therefore for tax years 2015-16 onwards, you will have a £40,000 overall annual allowance with a £10,000 limit on tax relieved money purchase savings.

You will not be able to carry forward any unused annual allowance from tax years prior to 2015-16 for any tax years from the year you first took a flexible drawdown payment.

Example 13

Edward took a payment of £75,000 through flexible drawdown on 1 March 2012. Since then, he has therefore had a nil annual allowance. He is a member of only one money purchase arrangement with a pension input period of 1 January to 31 December.

On 6 April 2015, his annual allowance for 2015-16 reverts to £40,000 with a £10,000 limit on tax relieved money purchase savings. His pension input period starting on 1 January 2015, will end in tax year 2015-16 so any savings to this arrangement in the period 1 January 2015 to 31 December 2015 will be tested against his 2015-16 annual allowance. He can therefore contribute up to £10,000 any time on or after 1 January 2015 to this arrangement without being subject to the annual allowance charge in relation to those contributions.

Are there any changes to the current recycling of tax free lump sum rules?

Recycling of a tax free lump sum involves using that lump sum as the means to increase contributions significantly to a registered pension scheme. The current recycling rule is intended to prevent the systematic exploitation of the tax rules to generate artificially high amounts of tax relief by using the tax free lump sum to make a further, tax relieved, contribution to a registered pension scheme. See RPSM04104920.

A change will be made from 6 April 2015, so that this rule applies where the amount of the pension commencement lump sum, taken together with any other such lump sums taken in the previous 12 month period, exceeds £10,000, not 1% of the lifetime allowance as at present.

If I have an annual allowance charge because my money purchase input is greater than £10,000, can I use scheme pays?

There are in effect no changes to when you can ask your scheme to pay your annual allowance charge in return for an actuarial reduction in your benefits.

Where your pension savings exceed £40,000 in a particular scheme and your annual allowance charge is greater than £2,000 (but based on the existing annual allowance calculation), you can require your scheme to pay the annual allowance charge in return for a reduction in your benefits.

You will not be able to require your scheme to pay any annual allowance charge if your total pension savings are less than £40,000, although they may do so on a voluntary basis, in return for a reduction in your benefits.

Chapter 4 Hybrid Arrangements

There are special rules for calculating the pension input amount for certain hybrid arrangements where the money purchase annual rules apply. However these rules are likely to apply only in a very limited number of cases.

What is a hybrid arrangement?

A hybrid arrangement is one where the decision on whether the benefits to be provided will be defined benefit, cash balance or other money purchase will be made at a later date. There are special rules for hybrid arrangements for valuing savings for the annual allowance. See RPSM06107050 for further information.

What are the special rules?

If you have triggered the money purchase annual allowance rules, then when working out whether a hybrid arrangement should be treated as a money purchase arrangement or a defined benefit arrangement, you must work out which gives the higher chargeable amount.

When are these special rules likely to apply?

They will only apply where you have a hybrid arrangement where the pension input amount calculated as if defined benefits were to be provided is higher than the input amount calculated if money purchase benefits were to be provided, as calculated under the normal rules in section 237 of FA 2004.

However, where you only have one, or even two, such hybrid arrangement the calculation will normally be straightforward as it will be clear what the chargeable amount would be if you used the money purchase amount rather than the defined benefit amount.

If your hybrid arrangement has a higher money purchase pension input amount than the defined benefit pension input amount, then this will always be included in the money-purchase pension input amount for the purpose of the money purchase annual allowance.

If it doesn’t then it could still be included in the money purchase pension input amount for the purposes of the money purchase allowance.

So what are the hybrid rules?

Where you have flexibly accessed your pension on or after 6 April 2015 then if you have one or more hybrid arrangements, you will have to work out separately the pension input

amount on each type of benefits that might be provided, and include in your annual allowance calculations the figure that would give rise to the highest annual allowance liability.

The rules only apply where you have a hybrid arrangement in which the pension input amount which would be used for annual allowance purposes under the normal rules is the defined benefits pension input amount (amount C) as opposed to the cash balance input amount (amount A) or the other money purchase input amount (amount B). See RPSM06107050 for pension input amounts under hybrid arrangements

You will need to calculate your default chargeable amount and your alternative chargeable amount taking into account all your arrangements, whether money purchase, defined benefit or hybrid arrangements.

The first step is to calculate the default chargeable amount. For this you first need to calculate your total pension input amount using the normal rules (see RPSM06107000). If this amount exceeds the normal annual allowance, (£40,000 plus any available carry forward), the amount of the excess is the default chargeable amount.

The second step is to calculate whether there is an alternative chargeable amount and if so its greatest possible amount. The alternative chargeable amount is made up of the excess of the defined benefit input amount over the alternative annual allowance (the normal annual allowance less £10,000) and the excess of the money purchase input amount over £10,000.

Extra steps are then needed to determine the alternative chargeable amount.

Where amount C is the same as or equal to amount A, amount B or the higher of amounts A and B (depending on the nature of the hybrid arrangement), the pension input amount for the defined benefit input subtotal is treated as a money purchase input amount for the purpose of establishing the alternative chargeable amount.

You then arrange these into as many differently-constituted sets of hybrid arrangements as possible, including a set with none of those arrangements within the set (that is an empty set). So for example, if there are two such hybrid arrangements, there are four possible differently-constituted sets.

You then work out for each of these differently-constituted sets what the money purchase input subtotal would be if the greater of amount A and B were used as the pension input amount for each arrangement within the set. You then use that figure in your calculation of the money purchase input sub-total (adding in any pure money purchase input amounts from other money purchase arrangements and non-relevant hybrid arrangements. You are then able to determine whether the resulting figure exceeds £10,000.

If it does not exceed £10,000, your chargeable amount is the default chargeable amount under the normal rules.

If it does exceed £10,000 you must then perform a further calculation. Taking each set in turn, you then work out the alternative chargeable amount based on each set. In doing so,

you include in the defined benefit input sub-total the Amount C for those hybrid arrangements that have been left out of that set. And you include in the money purchase input sub-total the amount A or B for those hybrid arrangements that have been included in the set.

You will then be able to compare the results for each set. The set which produces the highest figure will then determine which hybrid arrangements count as money purchase and which as defined benefit. You can then calculate the alternative chargeable amount accordingly. If this amount is more than the default chargeable amount, you are liable to the annual allowance charge on the alternative chargeable amount.

Example 14

Pavel has one arrangement which may provide either a defined benefit or an other money purchase benefit when he retires. Under the normal annual allowance rules, Pavel must therefore calculate the pension input amount as if the arrangement had been a defined benefits as well as an other money purchase arrangement. He determines his defined benefits pension input amount for the arrangement would be £15,000, whilst his other money purchase pension input amount would be £12,000.

If Pavel was not subject to the money purchase annual allowance rules, the £15,000 pension input amount for this arrangement would be tested against the £40,000 annual allowance as this is the higher figure.

However, Pavel has an old money purchase pension fund that he has not contributed to for a few years. Last year, Pavel has flexibly accessed those funds. This means he is now potentially subject to the money purchase annual allowance.

Pavel must therefore test the pension input amounts against the lower money purchase annual allowance as well as the normal annual allowance, to see which way gives the higher tax liability. He must work out his default chargeable amount and his alternative chargeable amount.

His default chargeable amount is nil, because £15,000 (as above) does not exceed £40,000.

His alternative chargeable amount is found by calculating any excess of the defined benefit input sub-total over £30,000, and adding to this any excess of the money purchase input sub-total over £10,000.

For the hybrid arrangement, it is the defined benefits total that would normally be taken as the pension input amount (because £15,000 exceeds £12,000). Because of this a further series of steps needs to be worked out.

Pavel has only one hybrid arrangement. There are therefore two possible sets, one containing the hybrid arrangement and one where the arrangement is left out of the set.

For the set containing the hybrid arrangement, Pavel has to substitute the money purchase input for the defined benefit input in that arrangement. So the money purchase input would be £12,000.

The set excluding the hybrid arrangement has no money purchase input, but a £15,000 defined benefit input.

Out of the two sets, only the first set results in a money purchase input over £10,000. So the alternative chargeable amount is worked out on this basis. The money purchase input for the hybrid arrangement is £12,000 and there is no input for the old money purchase pension fund. The money purchase input subtotal is £12,000, and this exceeds £10,000 by £2,000. There is no defined benefit input subtotal to add to this figure, so the alternative chargeable amount is £2,000.

£2,000 is more than the default chargeable amount of nil, so Pavel is liable for the annual allowance charge on £2,000.

Example 15

Angus has two arrangements which may provide either a defined benefit or an other money purchase benefit when he retires (hybrid arrangements). Under the normal annual allowance rules, Angus must therefore calculate the pension input amounts two ways, as if those arrangements had been defined benefit as well as money purchase arrangements, and see which gives the higher pension input amount.

Angus also has a defined benefit arrangement and a money purchase arrangement.

This tax year, Angus has flexibly accessed the money purchase funds. This means he is now potentially subject to the money purchase annual allowance rules.

	First Hybrid Arrangement	*Second Hybrid Arrangement*	*Money Purchase Arrangement*	*Defined Benefit Arrangement*
Defined Benefit PIA	*£20,000*	*£10,000*	*n/a*	*£15,000*
Money Purchase PIA	*£8,000*	*£4,000*	*£5,000*	*n/a*

Angus must therefore do certain calculations to see which way gives the higher tax liability. He must work out his default chargeable amount and his alternative chargeable amount.

His default chargeable amount is any excess of the total pension input amount calculated in the normal way over the normal annual allowance (£40,000). Angus's total pension input amount is as follows

£20,000 + £10,000 + £5,000 + £15,000 = £50,000

This exceeds the annual allowance by £10,000. So Angus's default chargeable amount is £10,000.

This process also tells Angus that both his hybrid arrangements have been taken for annual allowance purposes to be defined benefits arrangements. This means he has to go through the further steps to determine what is the highest possible chargeable amount in respect of those arrangements. He needs to calculate his alternative chargeable amount and compare it with the default chargeable amount.

His alternative chargeable amount will be found by calculating any excess of the defined benefit input sub-total over £30,000, and adding to this any excess of the money purchase input sub-total over £10,000.

Because there are two hybrid arrangements, there are therefore four possible sets, made up as follows –

Set one – the first hybrid arrangement only (leaving the second out of the set)
Set two – the second hybrid arrangement only (leaving the first out of the set)
Set three – the first hybrid arrangement and the second hybrid arrangement
Set four – leaving both of the hybrid arrangements out of the set.

For set one, the money purchase input sub-total would be
£8,000 + £5,000 = £13,000

For set two, the money purchase input sub-total would be
£4,000 + £5000 = £9,000

For set three, the money purchase input sub-total would be
£8,000 + £4,000 + £5,000 = £17,000

For set four, the money purchase input sub-total would be
£5,000.

Out of the four sets, set one and set three result in a money purchase input over £10,000. This means that those two sets go forward for the next stage of calculations.

Set one
Money purchase input sub total =£13,000 - £10,000 = £3,000
Defined benefit input sub total £10,000 + £15,000 = £25,000 - £30,000 = £nil
Total - £3,000

Set three
Money purchase input sub total = £17,000 – £10,000 = £7,000
Defined benefit input sub total = £15,000 - £30,000 = £nil
Total - £7,000

The higher of set one and set three is set three - £7,000. So this is his alternative chargeable amount.

£7,000 is however less than the default chargeable amount of £10,000, so Angus will be liable for the annual allowance charge on the default chargeable amount of £10,000.

Chapter 5 Where benefits have been taken at 5 April 2015

Any pension from a money purchase arrangement that you started to receive before 6 April 2015 will continue to be subject to the tax rules that applied before that date.

Lifetime annuity	See RPSM09101700
Drawdown pension	See RPSM09103500
Scheme pension	See RPSM09101400

As these pensions will be in payment at 6 April 2015, you will not be able to receive an uncrystallised funds pension lump sum from any of these pensions.

If you have designated funds into a capped drawdown pension fund under an arrangement before 6 April 2015, and that arrangement also holds uncrystallised rights, any further designations on or after 6 April 2015 will be to the existing capped drawdown pension fund, not to a flexi-access drawdown fund. The exiting tax rules (including the cap on pension payments) will continue to apply to those post 5 April 2015 designations. However you will be able to convert an existing pre April 2015 drawdown pension fund to a flexi-access drawdown fund.

Do the Money Purchase Annual Allowance rules apply to me?

The money purchase annual allowance rules will apply if after 6 April 2015 you

- designate funds into a flexi-access drawdown fund; or
- receive an uncrystallised funds pension lump sum.

They will also apply to you if:

- your pre 6 April 2015 pension is a flexible drawdown pension - the rules will apply to you from 6 April 2015; or,
- on or after 6 April 2015, you convert a capped drawdown pension into a flexi-access drawdown pension either by taking more than the permitted maximum for capped drawdown from a pre 6 April 2015 drawdown pension fund, or by electing to convert your drawdown fund to a flexi-access drawdown fund and taking a payment from that flexi-access drawdown fund.

The Money Purchase Annual Allowance rules will not apply if the only pensions you receive are one or more of the following pension types;

- A lifetime annuity;
- A scheme pension;
- A capped drawdown pension that has not been converted into flexi-access drawdown; or
- Any form of dependants' pension.

What happens if I take more than the permitted maximum from my pre 6 April capped drawdown pension fund?

If at any time during a drawdown pension year, the total amount you take exceeds 150% of the basis amount for that drawdown year, then immediately before the payment that will take you over the limit, your pre 6 April 2015 capped drawdown pension fund will automatically be deemed to be flexi-access drawdown fund.

This means that the payment that would have taken you over the limit, will be from the flexi-access drawdown fund, and so

- It will be an authorised payment and taxable as pension income, and
- It will trigger the money purchase annual allowance rules.

Can I change my pre 6 April drawdown pension fund to a flexi-access drawdown pension fund?

If your drawdown pension is a flexible drawdown pension it will convert automatically to flexi-access drawdown on 6 April 2015. The money purchase annual allowance rules will apply to you from 6 April 2015.

There will be two ways in which you can convert your existing capped drawdown pension into flexi -access drawdown

1. By taking more than the maximum capped drawdown pension. If the money purchase annual allowance rules don't already apply to you, they will apply to you from the date of the payment that takes you above the maximum capped drawdown amount.
2. By notifying your scheme administrator that you wish to convert the fund to a flexi-access drawdown pension fund. A notification can be made from the date of Royal Assent to the Bill but it will not be effective until 6 April 2015. If the notification is made on or after 6 April 2015 the fund will convert to flexi-access when your scheme administrator accepts your notification. The Money Purchase Annual Allowance rules will apply to you from the date you take a payment from your newly converted flexi-access drawdown fund, if they don't already apply to you.

A dependants' drawdown pension can be converted to dependants' flexi-access drawdown in the same way as a member can convert their drawdown pension to flexi-access drawdown. However as long as the individual has not received any form of member flexible access payment the money purchase annual allowance rules will not apply.

Chapter 6 Other Changes

A number of other changes have been included in the draft legislation as a consequence of the new flexibilities.

Small pots

From 6 April 2015, a payment of a small pot lump sum of up to £10,000 under;

- regulations 11, 11A or 12 of the Registered Pension Schemes (Authorised Payments) Regulations 2009 (SI 2009/1161); or,
- article 23C(4) of the Taxation of Pension Schemes (Transitional Provisions) Order 2006 (SI 2006/572),

can be made any time after the member has reached normal minimum pension age, that is age 55, or if the member has one their protected pension age under the protected pension scheme.

There will also be a change to regulation 10 of the Authorised Payments Regulations from 6 April 2015, so that from 6 April 2015, it applies where a payment could have been an authorised payment under regulations 11, 11A or 12 but for the continuance after the payment of an annuity. Currently this regulation applies where the payment could have been a trivial commutation lump sum but for the continuance after the payment of an annuity.

Trivial commutation lump sums

From 6 April 2015, a trivial commutation lump can only be paid from a defined benefit arrangement.

It will however be payable once the member has reached normal minimum pension age, that is age 55, or if the member has one their protected pension age under the protected pension scheme.

There is no change to how the member pension rights are valued to see if they are within the £30,000 triviality limit. All the member's rights under registered pension schemes, both money purchase and defined benefits, must be included in the valuation.

There is also no change in the requirement that the lump sum must extinguish all of the member's entitlement to benefits under the whole scheme - not just the defined benefits arrangement within it.

Trivial commutation lump sum death benefits

Where the member dies after the day on which Royal Assent is given to the Bill, a trivial commutation lump sum death benefit may also be paid to an individual in respect of any entitlement they had to receive any guaranteed payments of an annuity due to be paid after the member's death.

The limit for a trivial commutation lump sum death benefit is also being raised from £18,000 to £30,000 in respect of members who die after the day on which Royal Assent is given to the Bill.

Winding up lump sum death benefits

Schemes will no longer be able to pay a winding-up lump sum death benefit from the date Royal Assent is given to the Bill. All payments that could prior to this date be paid as a winding-up lump sum death benefit will still be able to be able to be paid from this date as an authorised payment, but as a trivial commutation lump sum death benefit.

Lifetime annuity paid before the member reaches normal minimum pension age

Where an individual becomes entitled to the payment of a lifetime annuity before their normal minimum pension age or retiring due to ill-health there are special rules for when the BCE occurs and how that BCE is calculated - see RPSM11104560. After 5 April 2015, the amount of the BCE2 in respect of that annuity at the member's normal minimum pension age will be the greater of;

- the sums and assets used to purchase the lifetime annuity and any related dependants' annuity; and
- the amount that would have been crystallised as a scheme pension to which the member became entitled at normal minimum pension age. That is, the annual rate of the lifetime annuity on that date multiplied by 20.

Pre A-day drawdown pensioners

The lifetime allowance was introduced from 6 April 2006 (A-day) but pensions in payment before A-day are not subject to the lifetime allowance charge. However, if and when the first benefit crystallisation event (BCE) on or after A-day occurs in respect of that individual, the pre A-day drawdown pension is tested against the lifetime allowance at that time for the purposes of working out how much lifetime allowance the member has available.

From 6 April 2015 the method of valuing a pre A-day drawdown pension will depend on the form of the drawdown pension.

Where the drawdown pension is a capped drawdown pension the value will be 25 times 80 per cent of the maximum annual amount that could have been paid as a capped drawdown pension on the date of the BCE.

Where before 6 April 2015 the pension is a flexible drawdown pension (see RPSM09103590), the value will be the 25 times the maximum annual amount that could have been paid as a capped drawdown pension at the point the member made the declaration for the pension to be a flexible drawdown pension. However if the flexible drawdown declaration was made in a drawdown pension year that began on or after 27 March 2014 the value will be 25 times 80 per cent of maximum annual amount that could have been paid as capped drawdown pension.

Where the drawdown pension is being paid from a flexi-access drawdown fund and prior to 6 April 2015 it was not a flexible drawdown pension, the maximum amount is 25 times 80 per cent of the maximum amount of capped drawdown pension that could have been paid at the point the member's drawdown pension fund became a flexi-access drawdown fund.

As the maximum that can be paid as a capped drawdown pension was increased from 120 per cent to 150 per cent of the basis amount for pension years starting on or after 27 March 2014, limiting the amount tested to 80 per cent of this figure ensures that overall the amount of lifetime allowance used up is the same as before 27 March 2014.

Example 16

Anil was taking pension as income withdrawal from a personal pension scheme before 6 April 2006. This is now a drawdown pension paid from a drawdown pension fund. Anil also has other pension rights that he hasn't yet crystallised. In December 2016 Anil crystallises the remainder of his pension rights, this is his first BCE. Anil has to value his pre A-Day drawdown pension.

Anil had not made a notification for this drawdown pension to be treated as flexible drawdown pension. However in May 2015, Anil notified his scheme administrator that he wanted his drawdown pension fund to be converted to a flexi-access drawdown fund. The calculation of Anil's maximum annual amount is based on the maximum drawdown pension at the point Anil converted his pension to flexi-access drawdown.

In May 2015 the basis amount of Anil's drawdown pension is £24,000. His maximum annual amount is 150 per cent of £24,000 (£36,000). Eighty percent of the maximum annual amount is £28,800. So the amount of lifetime allowance used up by Anils' pre A-day pension is: 25 x £28,800 = £720,000

Temporary periods of non-residence

The rules that apply for taxing flexible drawdown pension whilst temporarily non-resident - see RPSM09103620 - will be changed. From 6 April 2015 the types of pensions affected by these rules will be extended to include:

- Any drawdown pension (either as income withdrawals or short-term annuity) paid from a member's flexi-access drawdown fund
- Any drawdown pension (either as income withdrawals or short-term annuity) paid from a dependant's flexi-access drawdown fund
- The part of an uncrystallised funds pension lump sum that is taxable as pension income
- Any withdrawals from a drawdown fund or dependants' drawdown fund where individual was entitled to flexible drawdown pension before 6 April 20015.

The pension will only be taxed when the member become UK resident again if the total of relevant withdrawals during the period of temporary non residence was more than £100,000.

If any relevant pension is not paid in sterling it is to be converted into sterling equivalent by using the average exchange rate for the year ending 31 March for all payments in the tax year containing 31 March. The average exchange rates are published on the HMRC website at http://www.hmrc.gov.uk/exrate/yearly_rates.htm.

Similar changes are being made to the rules that apply where the payment was from a relevant non-UK scheme except that the amendments apply as if the payment had been made from a registered pension scheme

Scheme Rules Override

The rules of many pension schemes will not allow payments to be made using the new flexible access provisions. The legislation will include a permissive scheme rules override in connection with the following payments

- drawdown pensions;
- purchase of a short term annuity
- dependants' drawdown pensions;
- purchase of a dependants' short term annuity
- an uncrystallised funds pension lump sum

The scheme trustees or manager will be able to choose to whether or not to make any of these payments even if the scheme rules do not allow for this. Scheme trustees or managers will not be compelled to provide benefits using the new flexible access provisions.