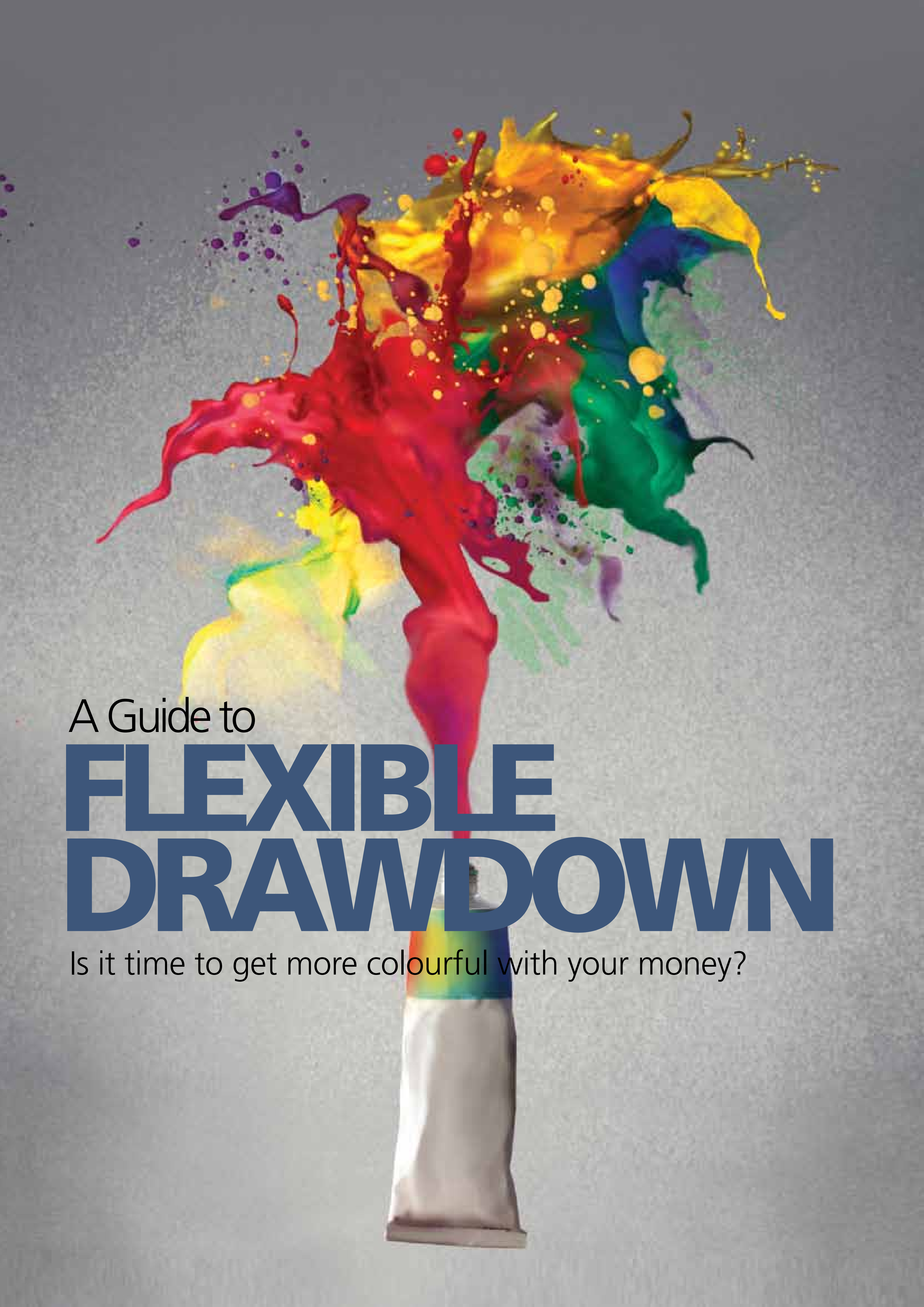

A Guide to

FLEXIBLE DRAWDOWN

Is it time to get more colourful with your money?

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Pension legislation is always on the move and keeping up to date with the latest changes could open up new opportunities for you in retirement. In April 2011, some of the most significant changes in pension legislation for five years were announced.

GAINING MORE CONTROL

Many of these changes were designed to limit what the Government clearly sees as over-generous tax relief concessions. But other changes have created the very appealing prospect, for people aged 55 or more, of gaining more control over when and how they can use their retirement savings.

Under the current rules, if you meet certain eligibility criteria, you can now take as much as you want from your pension, without the maximum income restrictions that apply to conventional drawdown arrangements. To be eligible for this facility – known as 'flexible drawdown' – you have to show that you already have a 'secure pension income' of £20,000 per year, in additional to your drawdown plan. This Minimum Income Requirement (MIR) is considered a safety net to prevent retirees draining their funds.

REGISTERED PENSION SCHEMES

Income from registered pension schemes count towards the MIR – such as lifetime annuities, occupational pensions, or the state pension. But income from pension schemes with fewer than 20 members, typically Small Self-Administered Schemes, will not count. You must also be already receiving the income for it to be counted – it cannot be based on future income.

As the name suggests this option is more flexible than income drawdown. Qualifying for this option removes the cap on the income you can take. There are no income limits at all and you can draw as much income as you like when you like. However flexible drawdown will not be available to everyone and there are certain criteria that must be met before you can choose it. It is also worth remembering any income is subject to tax at your highest rate.

ENHANCED DRAWDOWN FACILITIES

While, for many people, buying an annuity is likely to remain the most appropriate method of accessing their pension income, some will want to take advantage of these enhanced drawdown facilities.

Flexible drawdown could, for example, be used to meet one-off large expenditure items as they arise or to optimise your tax liabilities. It could also be a way to pass money through the generations, either by 'gifting' regular payments, for example into trusts, or as pension contributions to children using 'normal expenditure' rules so as to help avoid inheritance tax.

PAYING INCOME TAX

In moving money out of your pension fund before you die, you will be paying income tax on such payments but at a rate that is lower than the 55 per cent tax charge payable on a lump-sum payment from your pension fund when you die.

Another age-restricted benefit where the rules have been eased is the opportunity to take tax-free cash – typically a quarter of your pension pot – when you first start to take your pension benefits. Until April 2011, if you hadn't taken your tax-free cash by age 75, you lost the chance to do so. Now that restriction is removed too.

PENSION CONTRACT

Depending on your circumstances, all these changes may well sound like good news, but there's one important thing to be aware of. Just because the rules about when and how you take pension benefits have changed, it doesn't mean your pension contract will have changed as well.

If the terms of your contract have not been updated to reflect the new legislation, you could find that you can't take advantage of them. You could still find yourself obliged to buy an annuity at age 75. And if you haven't taken your tax-free lump sum at that age, you could still lose the opportunity to do so.

A pension is a long-term investment. The fund value may fluctuate and can go down as well as up. You may not get back your original investment. Past performance is not an indication of future performance. Tax benefits may vary as a result of statutory change and their value will depend on individual circumstances. This is for your general information and use only and is not intended to address your particular requirements. It should not be relied upon in its entirety and shall not be deemed to be, or constitute, advice. Although endeavours have been made to provide accurate and timely information, Goldmine Media cannot guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No individual or company should act upon such information without receiving appropriate professional advice after a thorough examination of their particular situation. We cannot accept responsibility for any loss as a result of acts or omissions taken in respect of any articles. Thresholds, percentage rates and tax legislation may change in subsequent Finance Acts.

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