Retirement Benefit Options

This booklet aims to outline the various options available when taking benefits from a pension, so you can feel better informed about the advice you are given and the decisions you make. It is intended for those who are both UK taxpayers and UK residents.

The options available will vary according to both the type of pension in question, and the rules of that specific scheme.

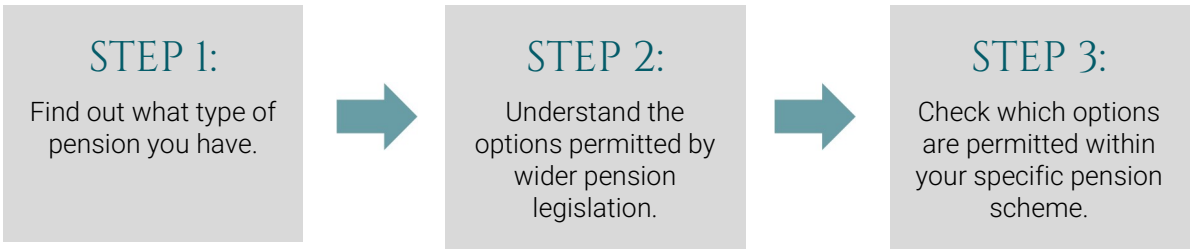
Last Updated: October 2023

Contents

Contents 2
Introduction 3
Types of Pension 4
Defined Contribution Pensions Overview 5
Defined Benefit Pensions Overview 5
When Can I Access My Pension? 5
Can I Change My Type of Pension? 6
Defined Benefits 7
When should I retire? 7
Should I take a lump sum? 7
Defined Contributions 8
Summary 8
Private Defined Contribution Pensions 9
What is an Uncrystallised Funds Pension Lump Sum (UFPLS)? 10
What is Flexi-Access Drawdown (FAD)? 11
What is an Annuity? 13
When Might Each Option Work Best? 15
A Final Note 15
Workplace Defined Contribution Schemes 16
What Might Be Considered a Valuable Benefit? 16
What is a Scheme Pension? 17
Other Ways of Accessing Pensions 18
Triviality Benefits 18
Serious ill-health 18
Conclusion 19

Introduction

This guide will cover the options available for each type of pension under current legislation, and you will need to check the type of pension you have and whether it can facilitate your preferred option (N.B. Transact pensions are private defined contribution pensions, and they can facilitate all the options); remember, just because pension legislation permits a certain option, a pension provider only has to facilitate the options permitted within the pension scheme's rules.



The first part of this booklet outlines the most common types of pension to help you with **step 1**; the next parts outline the various options permitted for each type under current legislation to help you with **step 2**. For **step 3**, you will need to either check with Lexington or your current pension provider.

If, during **step 3**, you find out your pension does not offer your preferred option from **step 2**, you can consider transferring it to a scheme that does offer it. This can be a complex decision so you should seek financial advice, and you should try to keep an open mind from the outset as transferring certain types of pensions may not be in your best interest. However, understanding all the options available under current legislation for the type of pension you hold will help you decide whether you might benefit from moving your pension elsewhere.

Types of Pension

Once you know what type of pension you have, you can skip to the relevant section of this document to understand the retirement options relevant to you.

Broadly speaking, your pension was either set up by you personally, or by your employer. 'Defined contribution' pensions can be set up by either you or your employer, and this document refers to the former as private defined contribution pensions and the latter as workplace defined contribution pensions; 'defined benefit' pensions will be set up only by an employer.

Defined Contribution Pensions

These are set up by you or your employer.

Common types of private defined contribution pensions include:

Personal Pension Plan (PPP)

Self-Invested Personal Pension (SIPP)

Common types of workplace defined contribution pensions include:

Group Personal Pension (GPP)

Section 32 Pension

Group Self-Invested Personal Pension (GSIPP)

Small Self-Administered Scheme (SSAS)*

*if you have a SSAS, you were likely involved in the set up but the scheme is linked to a company

Defined Benefit Pensions

These are set up by your employer.

Common types of defined benefit pensions include:

Final Salary schemes

Career Average Earnings schemes

There are numerous variations on the above, with pension providers often choosing to brand each of their various offerings with their own unique names.

Defined Contribution Pensions Overview

Your entitlement at retirement under a defined contribution pension is defined by how much money has been paid in, how that money was invested, and how those investments performed over time.

Defined contribution pensions are nowadays the most common type of pension, and generally they offer the most control and flexibility since you have a lot of options around if, how, and when to take benefits. Any benefits not used during your lifetime can usually be left (free of Inheritance Tax) to persons of your choosing.

The big drawback with these pensions is you bear the full burden of the associated administration, costs, and risks – most notably, if you do not pay adequate care and attention to the management of your pension, you could run out of money and have nothing left to help fund your retirement.

Defined Benefit Pensions Overview

Also known as a final salary or career average salary pension, retirement benefits are defined not by how much you contribute but rather by the length of your pensionable service with an employer and your pensionable earnings during that time. You may or may not be required to contribute to such a scheme, but these contributions are toward the cost of the scheme in general rather than your own specific benefits.

For most people, these are the gold standard of pensions, since all the costs, risks, and administrative requirements are borne elsewhere. If you have one of these pensions, you can be fairly certain of what you will receive and when, and that you will continue to receive it for the rest of your life; there is little for you to worry about. These benefits do give rise to some drawbacks but, for most, these are more than compensated for. There is a lack of flexibility around how much you receive and when – you can't switch payments on and off as needed, for example.

Similarly, the benefits for your loved ones in the event of your death are pre-defined and inflexible: most schemes will pay between one and two thirds of your entitlement to a surviving spouse, and some will pay a fraction of your benefit to any surviving children for as long as they remain financially dependent but, beyond that, you have no scope to leave any wealth to the next generation.

If you have no spouse or dependent children, the benefits die with you. If you anticipate a shorter lifespan, you don't have the option of taking a higher income to reflect this (in these circumstances some consider transferring their benefits to a personal pension, see the *Can I Change My Type of Pension* section).

When Can I Access My Pension?

In most cases, legislation permits access to your pension from the Minimum Pension Age, although scheme rules may dictate otherwise (particularly for defined benefit pensions).

At present, the standard Minimum Pension Age is 55, although it is set to rise to 57 in 2028 (this will affect most people born after March 1973); this change will not affect public service schemes for Firefighters, Police and the Armed Forces, and members of certain schemes prior to 4 November 2021 will also be able to access those benefits from age 55.

The rise is happening to correspond with the increase in the State Pension Age to 67. The Government has stated an intention to maintain the Minimum Pension Age at 10 years prior to the State Pension Age, meaning it could increase again from 57 if State Pension Age is increased in the future, but no automatic link exists yet so this would require specific legislation at the time.

If you are in ill health, it may be possible to access your pension sooner.

Can I Change My Type of Pension?

If you have a defined contribution pension, you should be able to change it into any other type of defined contribution pension currently available in the market, or any existing defined contribution pension you already have so long as it will accept new transfers in. For example, if you have a Personal Pension Plan (PPP), you could change it to a Self-Invested Personal Pension (SIPP) or transfer it into your workplace Group Pension Plan (GPP).

That being said, some older pensions offer valuable benefits not available to new investors, and these benefits are likely to be lost if you transfer the pension elsewhere. As such, you should proceed with caution – especially if you are thinking of moving an older pension set up by an employer, as these are more likely to have valuable benefits.

If you have a defined benefit pension, you should (with the exception of some Government schemes) be able to change it into any type of defined contribution pension available to you, however:

- Unless the pension is worth very little, you will need a financial adviser to do this for you.
- The adviser is required by regulation to start with the assumption you should not move your pension, and only advise you to move it if there are sufficiently compelling reasons to do so.

This is because the benefits offered under defined benefit schemes are very valuable, and the decision cannot be reversed once it is done.

It is not possible to change a defined contribution pension into a defined benefit one.

Defined Benefits

Generally speaking, the only choices you need to make are when to retire, and whether to take a lump sum.

When should I retire?

Most schemes will have a 'Normal Retirement Age' and for some schemes this will be fixed, giving you no choice in when to start receiving benefits.

If you do have the choice, taking benefits early will likely result in reduced payments, and taking benefits later will result in increased payments. You will need to consult with the scheme to understand how much the pension might change for each year you deviate from the Normal Retirement Age.

Retiring early is often beneficial if you have already finished your pensionable service – although the payments will be lower, you are likely to get more of them over time. By delaying retirement for a higher payment, you forgo all the payments you would have received between now and the day you retire.

Usually, members will have to wait until their late 70s/early 80s before the later retirement option becomes the more lucrative one, and most people would prefer to have the extra money in the earlier years of retirement whilst they still have the health and energy to enjoy it. However, there are some schemes where the early retirement penalty is sufficiently large that early retirement becomes a poor choice, so you will need to consider your own specific circumstances and do your own calculations (or seek financial advice).

Should I take a lump sum?

Again, some schemes won't give you the choice, but most schemes will offer 3 options, namely:

1. No lump sum with maximum income
2. Maximum lump sum with a reduced income
3. Any combination of lump sum/income in between options 1 and 2

The pension scheme will stipulate the rate at which you can swap income for a lump sum.

Provided you have adequate allowances available (£268,275 for 2023/24, although potentially higher for those with a valid Lifetime Allowance protection), any lump sum will be tax free, and the income will be assessable for Income Tax.

The lack of tax on the lump sum, plus the general preference for having more money in early retirement, tend to make the maximum lump sum the better option – you would usually need to wait until your mid-to-late 70s to be better off forgoing the lump sum, and if you choose to invest the lump sum at even a moderate level of risk it is unlikely you will ever be better off forgoing the lump sum. However, this will again depend on how much income you must give up for your lump sum, so you should consider your own circumstances and seek professional advice as needed.

Defined Contributions

The retirement options available within defined contribution pensions are markedly more complex than defined benefit pensions.

Summary

For those who preferred 'the sizzle, not the sausage', the below provides a high-level overview of the options available and the key points for each, with the following sections giving a much deeper dive. This section ends with some short examples of use cases, and how each option can be used to achieve the best outcomes.

TERM	DEFINITION
UFPLS	A single payment, or a series of payments over time, from your existing pension fund
FAD	Your pension fund remains invested but can pay you a flexible income
Annuity	You use your pension fund to buy a guaranteed income from an insurer

UFPLS

Up to 25% of the withdrawal is tax free.

- Completely flexible, can be regular or one off.
- You can leave anything left on death to your beneficiaries
- Requires more management and oversight.
- You could run out of money.

FAD

Up to 25% tax free lump sum at outset.

- Completely flexible; can provide regular or one-off withdrawals.
- You can leave anything left on death to your beneficiaries.
- Requires more management and oversight.
- You could run out of money.

Annuity

Up to 25% tax free lump sum at outset

- Guaranteed to keep paying for life (or shorter terms are available if needed).
- Easy for you to manage.
- Dies with you (unless you choose costly guarantees or death benefits at outset).
- Inflexible once set up.

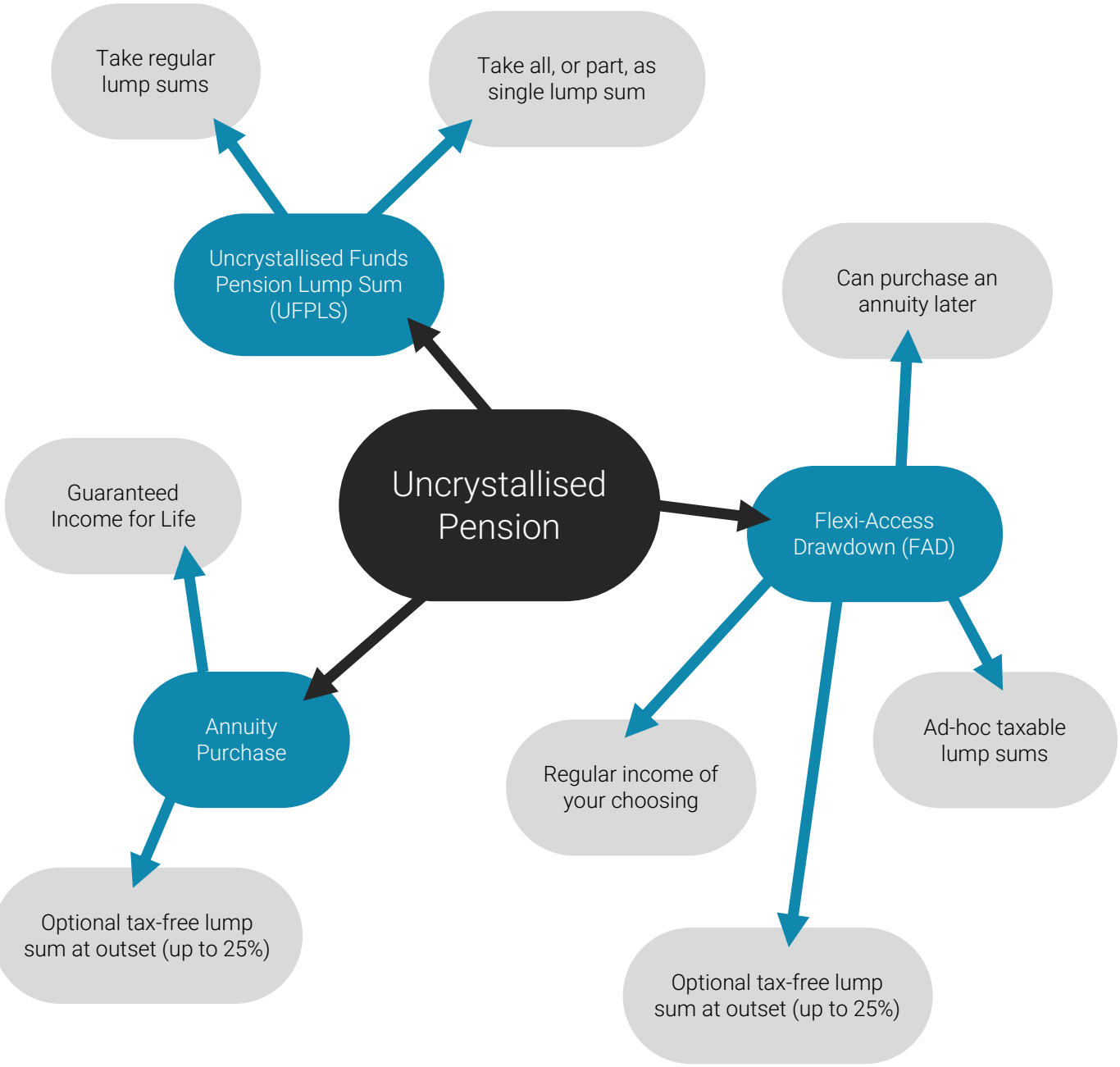
These options are not mutually exclusive; you can use some or all in varying combinations to achieve your required outcomes. You can also turn your pension into a FAD pot, and then later turn the FAD pot into an annuity, although you cannot turn an annuity back into a pension or a FAD pot.

Private Defined Contribution Pensions

Your untouched pension will be referred to as 'uncrystallised', or 'in accrual'. It will remain that way until you either access the pension or turn 75, whichever happens sooner.

There are 3 ways to get money out of an uncrystallised pot:

- Take some or all of the pension as an 'Uncrystallised Funds Pension Lump Sum' (UFPLS).
- 'Crystallise' some or all of the pension by turning it into a flexi-access drawdown policy.
- 'Crystallise' some or all of the pension by purchasing an annuity.



When crystallising defined contribution pension benefits (either by buying an annuity, or converting into flexi-access drawdown benefits), you have the option to take up to 25% of the crystallisation amount as a tax-free lump sum.

Up to 25% of a UFPLS payment will be tax free by default.

It is sometimes possible and desirable to set up regular (e.g. monthly) UFPLS payments and/or crystallisations into flexi-access drawdown.

You may also hear the term "capped drawdown", but this is a legacy arrangement so new money cannot be designated into a capped drawdown arrangement.

What is an Uncrystallised Funds Pension Lump Sum (UFPLS)?

Most schemes will let you take the entire pension as a UFPLS payment; more modern schemes will let you take as much or as little as you want.

Up to 25% of the lump sum can be paid tax free. There is a lifetime cap on the amount that can be taken tax free from a pension, so this is subject to you have sufficient tax-free allowance remaining; this rule looks set to remain in place, even as Lifetime Allowance legislation is dismantled.

The remainder will be paid to you by the pension provider via PAYE (just like a salary), with Income Tax deducted in line with the tax code provided by HMRC.

Under some circumstances, tax may be deducted on a 'week 1 month 1' basis, which will likely result in you paying far more tax on the withdrawal than you owe. If this happens, you will be able to reclaim the overpaid tax from HMRC. Pension providers have little control over the tax deducted via PAYE, as they must act in line with HMRC's requirements.

It may be possible to set up regular UFPLS payments, e.g. monthly, and this is often the best way to receive a flexible regular income whilst keeping your tax bill as low as possible.

As 75%+ of the lump sum will be assessed for Income Tax, this may not be the best option if you need a substantial one-off lump sum – you may pay less tax by crystallising enough benefits to provide the required lump sum tax free.

Any pension you do not access will remain invested and uncrystallised. The investments will need to be monitored and periodically reviewed, and there will be costs associated with the pension and any professional assistance you choose to seek in its management.

If you take more from the pension than it can sustain, its value will fall and once it reaches zero you will have no further entitlement to that pension.

Any value remaining in the pension on death can usually be left to your nominated beneficiaries (although this will depend to some extend on the scheme's rules).

What is Flexi-Access Drawdown (FAD)?

When crystallising benefits into a FAD arrangement, up to 25% of the value crystallised can be paid to you as a tax-free lump sum. As with the UFPLS, there is a lifetime cap on the amount that can be taken tax free from a pension, so this is subject to you have sufficient tax-free allowance remaining; this rule looks set to remain in place, even as the Lifetime Allowance legislation is dismantled.

The balance of the sum crystallised will be moved into a FAD pot (also referred to as a drawdown pot), where it will remain invested. The investments will need to be monitored and periodically reviewed, and there will be costs associated with the pension and any professional assistance you choose to seek in its management.

Access to the drawdown pot is completely flexible – you can take one-off withdrawals or set up regular (e.g. monthly) payments, either at outset or at any time in the future. Any withdrawals from the FAD pot will be paid to you via PAYE and assessed entirely for Income Tax in line with the tax code given to the pension provider by HMRC (which can create the same challenges outlined in the previous section on UFPLS payments).

In some instances, where possible, it can be advantageous to fund a one-off need by crystallising 4x the amount of money you need into a FAD arrangement. This means you get the money you need without paying any tax, your remaining accrual pot (and its 25% tax-free entitlement) can stay invested and continue to grow, and the FAD pot can also remain invested and continue to grow until you need it. This is better than crystallising the entire pot because it may result in a greater tax-free withdrawal overall, and it avoids needlessly increasing your Inheritance Tax (IHT) bill (which is what could happen if you take the full lump sum but do not spend all of it).

For example, if you need £10,000 from a £200,000 pension to fund a car purchase, you could crystallise £40,000 to provide a 25% tax-free lump sum of £10,000 with the remaining £30,000 remaining invested in a FAD arrangement for future use, and you'd also still have £160,000 in your accrual pot.

If your pension is sufficiently large, you can keep doing the above every time you need money until the pension is fully crystallised.

Any money in the FAD pot can be used to purchase an annuity at a later date if you wish, this may be useful if you need flexibility now but still want certainty later (e.g. if you are retiring at 60, but your State and Defined Benefit pension entitlements are not due until age 67 meaning you need more income in the earlier years until those pensions come into payment).

As the funds are already crystallised, there is no option to take a tax-free lump sum when using a FAD pot to purchase an annuity.

As with UFPLS payments, if you take more from a drawdown pension than it is able to sustain, its value will fall and once it reaches zero, you will have no further entitlement under that pension.

Any value remaining in the pension on death can usually be left to your nominated beneficiaries (although this will depend to some extend on the scheme's rules).

The UFPLS and FAD options have the following benefits and drawbacks:

BENEFITS

- Take only what you need when you need it.
- The balance can remain invested.
- You can switch withdrawals off and on as needed.
- With careful planning, you can minimise your tax bill.
- Anything remaining on death can be left to your chosen beneficiaries.
- You can still purchase an annuity at a later date with whatever is left.

DRAWBACKS

- You could run out of money before you die.
- Investments require ongoing management and oversight.
- Relatively complicated.
- May prove less lucrative than an annuity if you live many years into retirement.

You will trigger the MPAA the first time you:

- Take a UFPLS payment, or
- Take income from a FAD pot (not including the optional tax-free lump sum at outset)

If you trigger the MPAA, you will be limited on how much can be paid into your defined contribution pensions in the future. This limit is £10,000 per tax year as at 2023/24; this is reduced from the standard £60,000 (or your tapered Annual Allowance if lower).

Once the MPAA has been triggered, it cannot be undone.

What is an Annuity?

An annuity is where you use some or all of your pension to buy a guaranteed income from an insurer.

Essentially, you swap pension benefits for an insurance product, thereby relieving you of the costs and headaches associated with maintaining a pension (e.g. choosing and monitoring an appropriate investment portfolio) – this lack of administrative burden is a key advantage of annuities, although the main advantage is the guarantee.

Most annuities are guaranteed to last the rest of your life (although you can also opt for fixed-term annuities instead); with an annuity that is guaranteed for life, you know you will keep receiving a pension for as long as you live (unlike any drawdown arrangement, where it is possible to spend or lose your entire pension and be left with no income to fund your lifestyle).

This gives you certainty. Once your annuity is purchased, you know exactly what you will receive and when, and you can be certain of how that might change over your lifetime and what would be payable on death.

When purchasing an annuity, you will need to select the benefits you would like included. The types of options generally offered are:

- Spouse's benefit – you can opt for income to continue to be paid to your spouse after your death at a percentage of your income, e.g. 100% or 50%. If your spouse dies first, you do not benefit from this guarantee.

- Guarantee period – commonly 5 or 10 years, this guarantees that, if you die within this period, you'll receive a lump sum equal to the amount of income that would otherwise have been paid during the guarantee period had you not died.

- Payment frequency – you can choose how often you want to receive payments, e.g. monthly, quarterly or annually, and whether these should be made in advance or in arrears. Insurers often offer more income for lower frequency payments made in arrears, as it reduces both their administration and risk.

- Escalation – a level annuity will just pay you the same regular amount for the term of the policy, but you can choose to include escalation which will increase amounts at either a fixed percentage, e.g. 3% or 5%, or in line with some measure of inflation e.g. CPI or RPI – this helps maintain the real purchasing power of the annuity over time.

Guarantee periods, spouse's benefits and escalation are generally quite expensive – you pay via a reduced income entitlement at outset. The more benefits you add to an annuity, the less income you will be able to purchase (or the more it will cost to purchase your desired level of income), so there is a balance to be struck between income and peace of mind.

If you choose no guarantees and perish the day after the annuity is purchased, your custom will have been very lucrative for the insurer. Conversely, if the insurer expects you to live 20 years and you live for 30, you benefit at their expense. This aggregation of longevity risk is a large part of how insurers sustain their business – they know enough retirees will die relatively young to fund payments for those who die relatively old.

Once an annuity is in force, its terms cannot be changed. This is another key drawback of annuities – they lack flexibility. Some annuities are designed to incorporate an element of flexibility, but these are in the minority and the flexibility is likely to come at a cost.

The amount of income you are offered by insurers when purchasing an annuity will depend on a number of factors including the following:

- The value of the pension benefits funding the annuity.
- Your age at the time of purchase.
- Your health, medical, lifestyle, and history at the time of purchase (this is one of the few times it pays to be a heavy drinker and smoker, since this will likely result in higher payments).
- Your postcode (as this correlates with your expected longevity).
- Life expectancy statistics.
- The benefits you select at outset.
- Interest rates and gilt yields at the time of purchase.

The final bullet point largely explains why annuity rates have been historically low for over a decade now. This, coupled with greater levels of pension freedoms introduced by George Osbourne during his time as Chancellor, has caused annuities to fall out of favour in recent years. However, with interest rates headed back towards normality, annuities are offering better value again so these may become more appealing to many retirees.

Insurers underwrite different factors using their own criteria designed, in part, to compete with other insurers, so you should shop around to ensure you get the best deal.

If your health is seriously compromised, there are specialist annuity providers offering more income than standard annuities. If you think you might be eligible for such a policy, you should ensure you obtain appropriate quotes for your health condition.

Here is a summary of the benefits and drawbacks of annuities:

BENEFITS

- Guaranteed to keep paying so long as you live (unless you opt for a fixed term annuity).
- Certainty over what you will get and when.
- Optional guarantees and death benefits at outset.
- No administration once set up.
- Can select increasing payments at outset to help offset inflation (known as indexation).
- Simple, easy to understand.
- An annuity purchase does not trigger the MPAA

DRAWBACKS

- Adding guarantees, death benefits and indexation will increase the cost/reduce the amount of income you are offered.
- When you die, your beneficiaries will only receive the guarantees and death benefits you chose at outset.
- These will not enjoy the same inter-generational tax benefits of leaving an invested pension fund.
- You cannot add guarantees or death benefits once the annuity is in force, even if your circumstances change.
- You cannot take more or less than your monthly income.

When Might Each Option Work Best?

The following shows which options you might consider depending on the circumstances – please note, this is for guidance only and should not be considered advice; we would encourage you to seek financial advice before accessing your pensions in any capacity.

I need flexibility around accessing my pension

- Consider UFPLS or FAD; the best option will depend on your needs and tax position.
- Beware the Money Purchase Annual Allowance.

I need certainty around how much income I'll receive from my pension

- Consider buying an annuity.

I am a taxpayer looking for a one-off lump sum and nothing more

- Crystallise 4x the lump sum you need into FAD.
- Take the option of a 25% tax-free lump sum at outset.
- The remaining 75% will stay invested within the FAD pot, and you can take regular or one-off taxable withdrawals from this in the future.

I want to top up my income using my pension whilst minimising my tax liability

- Consider regular UFPLS payments.
- Or use FAD with a tax-free lump sum and use the lump sum to provide the income (e.g. by regular withdrawals from an ISA), rather than the FAD pot.

I want certainty, but need more income until my other pensions come into payment

- Consider using FAD now, then purchasing an annuity with the remaining pot once the other pensions are in payment.
- Or for more certainty, use part of the pension to buy an annuity now, and the rest to fund your additional needs until your other pensions are in payment.
- For the most certainty, you could combine a lifetime annuity with a fixed term annuity to provide the additional income until the rest of your pensions are in payment.

A Final Note…

The following section on workplace defined contribution pensions includes a section on valuable benefits, but these are not exclusive to workplace pensions. Although it is rare, older private pensions can carry these benefits too. It is always best to check this with the pension provider before accessing a pension, as this could sway your decision.

Workplace Defined Contribution Schemes

For defined contribution pensions set up by your employer, the options at retirement are likely to be much the same as for a private defined contribution pension, at least within the realms of the legislation. However, if the scheme was set up by an employer, there are a couple of additional things to consider:

- Employer schemes, especially older ones, are more likely to include valuable benefits.
- There may be one additional option, known as a 'scheme pension'.

The following sections elaborate on each of the above.

What Might Be Considered a Valuable Benefit?

Valuable benefits are rare, but we do still see them from time-to-time. They are not all exclusive to workplace pensions, but this is where they are more commonly seen. These could include:

- An entitlement to a tax-free lump sum of more than the standard 25% (there have even been schemes that permitted a 100% tax-free withdrawal).
- Guaranteed Annuity Rates (GARs), i.e. the option to purchase an annuity at a fixed rate not determined by macroeconomic factors (and these are often far more lucrative than those available on the open market), or guaranteed fund values which guarantee your pension will be worth at least £x on a given date.
- Guaranteed Minimum Pensions (GMPs) – if you contracted out of the State Pension, your workplace pension (be it defined benefit or defined contribution) had to guarantee at least a minimum level of income to compensate for your reduced State Pension, which could be more than you'd have been able to receive otherwise.
- Protected Minimum Pension Age – if you were a member of certain schemes prior to 6 April 2006, you may be able to access your pension before the Minimum Pension Age; similarly, if you were a member of certain schemes prior to 4 November 2021, you may be able to access your pension from age 55 even after the Minimum Pension Age has increased to 57.

The common drawback is the scheme is unlikely to provide all the options available with more modern schemes at retirement and on death; some very old schemes even mean the pension would form part of your estate for Inheritance Tax (IHT), unlike modern schemes (and this can be easily missed, meaning your IHT bill could be far higher than expected).

For example, a pension may permit you to take up to 50% of its value as a tax-free lump sum, instead of the usual 25%, but it might compel you to purchase an annuity with the remaining 50%. Whilst an annuity purchase might not have been your preferred option, most people will accept this for the tax saving on the enhanced lump sum. Of course, if you desperately wanted to use drawdown, you could always consider transferring the pension to a more modern scheme, but you would lose the entitlement to the higher tax-free lump sum.

Some of the benefits available under old workplace schemes are so valuable they would be treated in the same way as a defined benefit pension if you wanted to transfer them elsewhere, i.e. you would need a financial adviser to transfer it for you, and there would need to be sufficiently compelling reasons to do so.

What is a Scheme Pension?

A scheme pension is essentially an annuity policy provided by the pension scheme, instead of an insurer. These are relatively rare.

The scheme will usually stipulate the parameters of the scheme pension, which are generally favourable compared with open market annuities, although they may not offer all (or any) of the options available when purchasing an annuity on the open market. In this way, scheme pensions are something of a mixture between a defined contribution and a defined benefit pension – in accrual, they look a lot like the former, but in retirement they look more like the latter.

Other Ways of Accessing Pensions

There are more ways of accessing pensions, but these only apply in very limited circumstances. As such, these are only covered briefly as they are not available to most retirees, but it is important you are aware in case one of the options is available to you.

Triviality Benefits

If the value of your pension benefits is considered trivial, the pension can be taken in full as a lump sum using one of the following options:

Rule	Scheme type	Threshold
Small pot lump sum	Defined contribution and defined benefit schemes	£10,000
Trivial commutation lump sum	Defined benefit schemes	£30,000
Winding-up lump sum	Workplace defined contribution schemes	£18,000

These are essentially taxed as UFPLS payments (i.e. 25% tax free, the remainder taxable as income), but with the added advantage that they do not trigger the MPAA or use any lifetime allowance (although it remains to be seen whether they will count towards the allowances governing tax-free lump sums that look set to replace the lifetime allowance). You can receive up to three of these payments during your lifetime.

To qualify for the rule, the value of your pension benefits must be less than or equal to the threshold amount for that rule. The winding-up lump sum is, perhaps obviously, only available if the scheme is being wound up. The lump sum must extinguish all your rights under the arrangement (for small pot lump sums from private personal pensions) or scheme (for everything else).

Whilst the £30,000 threshold for trivial commutation lump sums may appear more generous than the small pots limit, it is important to note this value includes pension rights in all schemes, including any personal pensions, workplace defined contribution schemes and schemes already in payment. The method of valuing a defined benefit entitlement is to multiply the yearly pension by 20 and add any separate tax-free lump sum.

Serious ill-health

As well as the normal ill-health retirement benefit options (which allow access before the usual Minimum Pension Age, currently age 55), if someone has a life expectancy of less than a year it may be possible for uncrystallised funds to be paid entirely as a tax-free lump sum (known as a serious ill-health lump sum).

Any benefits already crystallised will continue to be paid as a taxable income.

You should also consider the Inheritance Tax implications, as any lump sum not spent on death will form part of your taxable estate.

Conclusion

As you can see, there are many options to consider at retirement and no 'one size fits all' approach; some might say the range of options and the pitfalls make retirement a minefield in which a little bit of knowledge can be a dangerous thing.

It should go without saying that we recommend employing the services of a financial planner before accessing any pensions – even if you only use a financial planner once in your life, this is probably the time to do it.

Hopefully, this document will allow you to arrive at your financial planner's offices armed with a good level of basic knowledge, so you can make informed contributions to your plan and be comfortable with the pros and cons and the alternatives available.

If you feel there are any aspects of taking retirement benefits this guide has overlooked, please get in touch – we'd love to hear from you about how it might be improved.