CURTIS BANKS

CASE STUDY

PCLS (TAX FREE CASH) AFTER AGE 75

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Please note: for simplicity, this case study assumes a standard lifetime allowance of £1.03m throughout. However, under current legislation the standard lifetime allowance is set to increase each tax year in line with increases in the Consumer Price Index (CPI).

An investor is confused about whether she can take tax free cash after turning age 75, and how her entitlement will be calculated.

The Challenges

Margot is 74. She recently took some benefits from her pension for the first time. Margot made sure that she paid into a pension whenever she could throughout her life, but had never really paid much attention to the rules about taking money out of one before. However, once she started thinking about her options, she found researching the rules quite interesting and now feels she has a good understanding of some of the basic concepts.

Margot opted to crystallise £430,000 from her pension, taking £107,500 as a pension commencement lump sum (PCLS) and putting £322,500 into drawdown. Her pension provider told her that she had used 41.74% of her lifetime allowance. Margot's remaining uncrystallised pension benefits are currently worth £600,000.

Margot understands from her reading that each time she crystallises some of her pension benefits, she can take a quarter of the amount as PCLS. She also understands that the maximum amount of PCLS she can have in total is a quarter of the lifetime allowance. Therefore she reasons that at any given time, her overall remaining PCLS entitlement should be a quarter of her remaining lifetime allowance entitlement.

However, Margot has just received a letter from her pension provider to confirm that her pension will be tested against the lifetime allowance on her 75th birthday in a few weeks' time. Margot is now confused: her remaining uncrystallised funds will use up her remaining lifetime allowance. Does that mean she will lose her remaining PCLS entitlement unless she withdraws it before she turns 75? Margot can't remember reading anything to this effect, but decides to call her pension provider to check.

The Actions

Margot calls her pension provider. The representative, Toby, is happy to talk through the rules with Margot, but he also confirms that he won't be able to offer any advice and recommends that Margot speaks to an adviser if she wants to talk about her situation specifically and what might be best for her.

First, Toby clarifies exactly what will happen on Margot's 75th birthday. He tells her that the value of the uncrystallised funds will be tested against the lifetime allowance, as well as any growth in the crystallised funds. If there is any excess over the lifetime allowance, the provider will deduct a 25% lifetime allowance excess charge and send this to HMRC. Margot is not overly concerned about her pension growing significantly in the short time left before her birthday; she is sure she will only be a few pounds over or under the allowance.

Secondly, Toby tells Margot that she will not lose her remaining PCLS entitlement when she turns 75. Toby confirms Margot's understanding that her remaining PCLS entitlement is a quarter of her remaining lifetime allowance, but also that this works slightly differently after age 75. From then on, her remaining lifetime allowance for this purpose is found by ignoring the tests at age 75 and including any other amounts which have been crystallised after age 75.

The Results

The value of Margot's pension had only changed fractionally by her 75th birthday, and the tests used up the remaining 58.26% of her lifetime allowance.

A couple of years later, Margot's uncrystallised funds (which she learns are technically called 'unused' funds now she is over 75) have increased in value to £700,000. Margot decides to crystallise another £200,000.

Thanks to Toby, Margot understands that her remaining overall remaining PCLS entitlement is the lifetime allowance (£1.03m) less the amount she crystallised before turning 75 (£430,000) divided by four:

(£1.03m - £430,000)/4 = £150,000.

Therefore Margot is confident that from her £200,000 crystallisation she can take £50,000 PCLS and put the rest into drawdown. Her pension provider confirms this is correct and processes the crystallisation.

The following year, the remaining unused funds are still worth £500,000 and Margot decides to crystallise the whole amount.

This time, Margot knows she needs to deduct the amount she crystallised last year as well as the amount from before her 75th birthday to find her remaining PCLS entitlement:

(£1.03m - £430,000 - £200,000)/4 = £100,000.

Margot understands that even though a £500,000 crystallisation would normally allow for £125,000 PCLS, she will be limited by her remaining overall entitlement of £100,000.

Margot wonders if she will need to pay a lifetime allowance charge, as this must mean that her pension has grown above the lifetime allowance. However, when she calls her provider, a representative confirms that there are no more lifetime allowance tests for her pension after age 75, and the rest of her £500,000 crystallisation will simply go into drawdown.

Contact Details

If you'd like to speak to us about anything on this fact sheet, please contact us on:

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