CURTIS BANKS

FACT SHEET

DRAWDOWN

APPROVED FOR CLIENT USE | APRIL 2025

Definitions

What is drawdown?

Drawdown is one of the main ways of accessing your pension benefits. In drawdown, you keep your pension fund invested and take income payments directly from it. You can carry on investing the money in the pension and will benefit from any investment growth; however, if there is investment loss this directly affects the pension benefits available to you. You can choose to start and stop income payments at any time. This is considerably different from an annuity, which involves using your pension fund to buy a regular income, normally for life, from an annuity provider.

There have been three types of drawdown: capped, flexible and flexi-access.

What is capped drawdown?

Up until 6 April 2015, this was the most common form of drawdown. In capped drawdown, individuals receive a maximum income limit which restricts the amount of income available each year, in order to minimise the risk of the pension fund running out during the individual's lifetime.

It's no longer possible to begin a new capped drawdown plan, but you may still have funds in capped drawdown which began before 6 April 2015.

What is flexible drawdown?

Flexible drawdown was available between April 2011 and April 2015. Unlike capped drawdown there was no maximum income limit in flexible drawdown. However, it was only available to individuals who already had sources of guaranteed income – in other words, who didn't need the fund to last for their lifetime.

Flexible drawdown no longer exists – on 6 April 2015 all flexible drawdown plans were converted to flexi-access drawdown.

What is flexi-access drawdown?

Flexi-access drawdown is the newest type of drawdown and the only one available to new drawdown customers. It was introduced on 6 April 2015. Like flexible drawdown, there are no income limits for customers in flexi-access drawdown, but unlike flexible drawdown, it is available to anyone.

Rules

How does capped drawdown work?

If you were already in capped drawdown before 6 April 2015, you can stay in capped drawdown and the same rules apply. You may also be able to designate further funds into your existing capped drawdown fund.

You can convert to flexi-access drawdown if you like, but this choice is irreversible and may affect your options for saving into a pension in the future.

SL156.202504
April 2025

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When you first put funds into capped drawdown, your provider would have calculated your maximum annual income limit. The calculation takes into account factors such as the fund size and your age, and is based on a table of rates prescribed by the Government Actuary's Department.

Your income limit is the most you can take each 'drawdown year', which is the 12-month period after you first put funds into drawdown and each 12-month period after that.

Income limits are currently recalculated every three years until age 75 and annually thereafter.

If you put more funds into an existing capped drawdown fund, the income limit is recalculated at that point. You can also request early income limit reviews, but only at the end of a drawdown year.

What happens if I switch from capped drawdown to flexi-access drawdown?

If you switch from capped drawdown to flexi-access drawdown, you will no longer have an income limit and therefore no more income limit reviews.

When you take your first income payment in flexi-access drawdown, you will trigger the money purchase annual allowance (MPAA). This will reduce the amount you can contribute to money purchase pensions each year while benefiting from tax relief from £60,000 to £10,000. You can find more information about this in our MPAA fact sheet. We would recommend speaking to an adviser before switching from capped to flexi-access drawdown if you may still need to build up further pension funds in the future.

Income from a capped drawdown plan does not trigger the MPAA.

How does flexi-access drawdown work?

If you put funds into drawdown for the first time from 6 April 2015 onwards, they will go into flexi-access drawdown. There is no limit on the amount of income you can take each year from your flexi-access fund, but bear in mind that there may be tax implications if you take a large payment.

How is drawdown income taxed?

Any income you take, whether from capped or flexi-access drawdown, is subject to income tax. When you take your first income payment from a particular provider, they have to use an emergency rate tax code, unless you can provide evidence of your tax code such as a current P45. Emergency tax codes assume that the payment will be the first of a regular series and make assumptions about factors such as your personal allowance, so they can result in you overpaying or underpaying tax.

Once the first payment has been made, HMRC will send your provider your tax code to use for future payments. If you are beginning to take a regular income, this tax code will normally correct any over or underpayment from the first income payment. If you took a single income payment, HMRC may write to you at the end of the tax year to return any overpaid tax, or request money from you if you underpaid. Alternatively, you can contact HMRC during the tax year to correct any problems.

What if I want to change my pension benefits or move to a new provider?

If your funds are in capped or flexi-access drawdown you can still use them to buy an annuity. You can use some or all of your drawdown fund for that purpose.

You can also still transfer your drawdown funds to another pension provider, although you can only move a whole drawdown 'arrangement'.

If the benefits you want to transfer were all put into drawdown with the same provider, these will often be part of the same arrangement. You'll need to check with your pension provider to make sure though, as some providers open a new arrangement each time you access some of your benefits.

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Important points to consider

The value of pension funds may fall as well as rise. Your money is tied up until you take your benefits. Benefits can generally be taken any time after age 55, although this is due to increase to 57 in 2028.

This information is based on our understanding of current legislation, including (but not limited to) FCA, PRA and HMRC regulation. It does not constitute any form of advice.

Contact Details

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