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READERS: PLEASE ALSO NOTE LATER UPDATE SHEET 16 February 2016 ON ACA WEBSITE

05 June 2015

By email to ptm.consultation@hmrc.gsi.gov.uk

Dear Sirs

Pensions Tax Manual - inclusion of examples on the use of UFPLS and its interaction with PCLS
Letter 1 – standard member with NO protections (and in particular no scheme specific protected lump sum limit

This is the first of two letters on related subjects, written with the draft Pensions Taxation Manual (PTM) released in March 2015 in mind. We know that you aimed to get all input on this by the end of May but hope you can take this letter into account in time for your next issue (ie the first version in final).

The example in this letter relates to a member of a scheme who has

- DB benefits as his main arrangement
- but also has a DC fund alongside in this case arising from AVCs.
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The scheme policy in the past has been to allow/require all/any PCLS to come from the DC fund first - quite a common policy.

- If there is scope for more PCLS, this can be granted by way of commutation of DB pension;
- if instead the AVC fund is larger than the scope for PCLS then in the past the balance of the funds have had to provide additional pension (either by way of annuity purchase or internal conversion to scheme pension).

In the post 2015 world of Freedom and Choice, the Trustees are minded to continue this policy with one variation – that if the AVC funds are bigger than the PCLS that is supported by the DB pension and the PCLS itself ie the last bullet above, the trustees will also offer the member the opportunity to "cash out" all the excess AVCs, so the AVCs are partly delivered as a taxed lump sum.

The Trustees are minded to do this using the UFPLS route (although they could use other routes such as allowing the member to designate funds to Flexi Access Drawdown and draw all that as income in one go).

The example in this letter shows one valid route that the Trustees could choose to take (subject to what their scheme rules permit), **for a standard member with no protection, and in particular with no scheme specific protected lump sum limits,** with the same amount of AVCs being treated as tax free .

We would really appreciate
(a) Your confirmation that you agree with our reading and
(b) Your inclusion of these examples in the PTM to give help on what is a common benefit structure.

For your information, given the topicality of this issue, we will be putting this letter onto the ACA website where it is available to the general reader. **If you think that there is anything flawed in what we have shown here, it would be very helpful if you were able to let us know early.**

Best wishes

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APPENDIX

Example - a “standard” member with no protections

Data: John has no lump sum protection.
He has a pension entitlement of 10K pa and an AVC fund expected to be £120K (but the exact amount will be finalised when it is disinvested just before drawing). He does not have any Lifetime Allowance protection or LTA enhancement and he is well below age 75.

The scheme rules allow the Trustees to pay maximum levels of PCLS.

Had the 2015+ flexibility not been introduced, he would have been offered two options under the scheme rules:

- To take all benefit as pension, with the Trustees using the AVC fund to buy a lifetime annuity of his choice.

- To take PCLS up to the maximum from his AVCs as follows:

  drawing PCLS from his AVC funds of £66,666 (= 20/3 x £10,000) “in connection” with the DB pension of £10,000 pa (because £66,666 does not exceed 25% x (66,666 + 20 x 10,000); and

  taking the balance of the AVCs 75% as annuity purchase and 25% as further element of PCLS.

  So if the final AVC total balance is indeed £120K and hence the remaining balance is £53,333 after the element of the PCLS supported by the DB pension (and itself), that would mean £40,000 would be used to buy an annuity and £13,333 as a further PCLS element.

  The total PCLS in this case of £80,000 ties in with the formulae identified in RPSM09104490* (as used with the substituted text applying under “Applications” there and hence with formula A applying). If the fund is different from £120K when realised, this just means that the balance is different – but still can be delivered as 75% annuity purchase and 25% PCLS.

However, given the 2015+ tax law changes, the Trustees are minded to allow James an option that does not require him to have the balance of his AVCs used to secure annuity income.

Under the new UFPLS provision introduced by TOPA2014,
the Scheme could for example introduce the following further option, which would result in the member being able to access the same amount of AVCs tax free and the remaining AVCs as taxed cash.

- drawing PCLS from his AVC funds of £66,667(= 20/3 x £10,000) “in connection” with the DB pension of £10,000 pa; and
  Drawing the balance of the AVCs £53,333 an UFPLS which will be 75% taxable (£40,000) and 25% tax free (£13,333). It will all be paid through payroll and subject to the PAYE deduction process.

  The UFPLS BCE date will be its date of payment. The outcome will generally be the same whether the UFPLS BCE counts as having its BCE date before or after the DB pension and associated PCLS BCEs, unless the member is close to the Lifetime Allowance in which case the order of BCEs may matter.

***** *We note that this section of the RPSM has not been carried over into the PTM and we hope that the text can be reinstated, as it is a very useful section and example set.*