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John Dingle & Patricia Lynch
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Dear John and Patricia,

John Dingle Project Planning Ltd Retirement Benefits Scheme

I refer to our email correspondence in connection with the drawdown of benefits from this plan, having regard to the financial review presently being undertaken by Simon Claxton.

The objective of this letter is to consider the merits and conditions of flexible drawdown to allow John to draw his pension from the scheme without any restriction on the maximum that can be taken.

Presently, the fund is un-allocated, which means that the trustees have complete discretion on how funds are apportioned to any beneficiary of the plan. The plan operates as a discretionary trust, giving the trustees absolute flexibility in how pension assets are paid and allocated.

Pension Income Options

Pensions can be paid in one or a combination of the following ways:

With a drawdown pension you can choose how much pension you want to be paid each year. You can change the amount you receive and a pension scheme does not have to pay pension in the form of a drawdown pension. You can have your drawdown pension paid

- directly from the scheme,
- from an insurance company using a short-term annuity, or
- as a mix of payments direct from your scheme and from a short-term annuity.

Drawdown comes in two forms - **capped drawdown** and **flexible drawdown**. So in practical terms drawdown pension can be paid one or more of three ways

- capped drawdown
- flexible drawdown, or through a short-term annuity.

You start a drawdown pension by ‘designating’ part or all of your pension funds to provide you with a pension. The funds that you have put aside (designated) to provide a drawdown pension will form your ‘drawdown pension fund’.

With capped drawdown there is a limit on the amount of pension you can take from your scheme each year. This limit is regularly reviewed; based on a pension fund for John of a fund of £1,038,428 (as per the most recent accounts) and after taking a lump sum of £259,607, the pension income payable would be £44,860 p.a. from the scheme.

With flexible drawdown there is no limit on the amount of drawdown pension you can take each year. You can take as much or as little as you like. There is also no need for your pension fund to be reviewed. However you must receive a pension guaranteed of £20,000 p.a. to qualify for flexible drawdown.

Actuarial Cost

To qualify for a pension guaranteed of £20,000 you must be in receipt of one or more income from the following sources:

- State pensions
- Lifetime annuity
- A scheme pension

As John is not at this time in receipt of a state pension, one must only consider a lifetime annuity or scheme pension.

Lifetime annuity

Under the lifetime annuity option, the present rates to secure a non increasing annuity amounts to £390,160, which has been prepared on the basis as the lowest cost of annuity in the market relative to the fund. This would give a single life pension non increasing each year of £20,000 and as such would leave £388,661 in the plan all of which could be taken in one of more installments until the plan is exhausted and wound up.

Given John’s health, I would expect that we could secure improved terms, which would reduce the purchase price from £390,000; but would not be significant. For the record, the cost to the scheme if you required a 3% increase each year for the annuity of £20,000 would require an additional fund of £206,591. This is reflective of the low interest rates and John’s age.

In summary, after taking your tax free cash of £259,607 you will need to use £390,160 of the remaining fund left in the SSAS to purchase a £20,000 pa annuity, which would allow you to draw the remaining funds in the SSAS at no minimum or capped amount. You will pay income tax on that drawdown.

Scheme Pension

Scheme pension – up to the Finance Act 2011, the trustees could have utilised scheme pension which is a guaranteed pension payable from the SSAS but one which has not been annuitised. It is guaranteed in that it is a debt on the trustees of the plan – but as you are the trustees, the debt is meaningless in that they would be taking legal action on yourselves to enforce this.

We have widely used scheme pension as a tax efficient method of pension income, unfortunately following lobbying by the SIPP industry scheme pension is no longer available to SSAS as a defined contribution arrangement.

It is however available as a defined benefit plan and as such needs to be considered as an alternative to annuitising £390,160 to secure a £20,000 pa income.

We have had an actuarial cost undertaken of what amount of fund would be required to secure a scheme pension of £20,000 as a defined benefit pension plan. This cost amounts to £421,221, and therefore this would leave £357,600 in the current SSAS to draw as you deem appropriate.

In practical terms, under scheme pension the trustees would "allocate" £421,221 into a separate pension arrangement under the SSAS called a defined benefit arrangement. The trustees would pay out £20,000 a year as pension income and would be free to draw the balance in the current non-defined benefit part of the SSAS along the lines stated.

On death, the balance of funds in both schemes would be used to pay a spouse's pension until second death. Any remaining funds in the defined benefit arrangement on second death would be refunded back to the Company sponsoring the plan less a tax charge. In respect of the defined contribution part, the balance of any funds remaining would be paid to beneficiaries less a 55% tax charge. There are some additional options that apply in respect of death benefits and certainly tax planning can be undertaken which can be covered under a separate letter.

At the time of writing, the scheme pension option is an expensive one in that it requires the trustees to utilise over half of the remaining fund into a separate defined benefit arrangement. In addition, a Finance Bill due to take Royal Assent in the summer whereby the scheme pension option I have described will only be available where there are 50 or more members in the plan is proposed. It is likely to be passed and may have retrospective effect;

as HMRC are presently issuing this new condition as a “practice note”. I have been in touch with HMRC technical and am awaiting further clarification on this matter as it is not set in stone at this time.

You may therefore wish to consider taking maximum drawdown under “capped” pension income of £44,860 p.a. and dispose of other assets outside the SSAS to increase your monthly income.

Alternative Option

I have made separate enquries in respect of a lifetime annuity via the Channel Islands under the Cavendish Lifetime annuity; this allows the trustees to drawdown a pension by transferring part of the SSAS overseas which would pay out an annuity at the rate of £20,000 pa but unlike a conventional annuity, the death benefits can be distributed as a capital sum or income without setting aside a pension reserve. The reason that there would be a return of capital sum under death benefits is that the funds are ring-fenced in a protected cell structure. It is approved by HMRC. Cavendish are a regulated firm and I am aware that this has been successfully used for a number of years prior to the recent Finance Bill. I am awaiting clarification from Cavendish whether their “annuity” conforms with current HMRC regulations and as such could be appropriate for you.

I appreciate that there is a lot to consider here and I need a response from Cavendish and HMRC before issuing my final guidance on this. If you, John and Simon wish to have a conference call to talk this through please do let me know.

Yours sincerely

Gavin McCloskey
For Pension Practitioner .Com

Enc

Cc Nikki Spoor