Lifetime Allowance (LTA) at age 75 case study

The Challenges:

Brian will turn 75 on 1 March 2019.

Brian has three pensions. One is still uncrystallised and currently worth £381,100. The second is in flexi-access drawdown: it was originally crystallised in May 2009 and is currently worth £651,250. The third is also in flexi-access drawdown and was originally crystallised before 6 April 2006 (A-Day). Brian has tended to take income from this plan over the years and it is currently valued at £100,000.

At face value Brian's pensions are over the LTA, but it's not quite that straightforward when crystallised funds and pre A-Day pensions are involved.

The Actions:

Firstly, check how much lifetime allowance Brian has available for the age 75 test. The records show that the second pension was worth £525,000 when it was crystallised in May 2009. The LTA was £1.75m at the time, so this used 30% of the LTA. The pre A-Day pension was valued at £350,000 at the time for LTA purposes, using a further 20%. Therefore, Brian has 50% of his LTA available.

There are three separate Benefit Crystallisation Events (BCEs) which can take place at age 75:

- BCE 5 tests funds in a defined benefit arrangement which have not yet been crystallised
- BCE 5A tests any growth in a drawdown pension
- BCE 5B tests uncrystallised funds in a money purchase pension

Brian does not have a defined benefit pension, so only BCE 5A and 5B apply.

The uncrystallised pension is the simplest; assuming the fund value of £381,100 stays roughly the same, it will use approximately 37% of the lifetime allowance, which will be £1.03m on Brian's birthday.
The second pension is now worth £621,250, but only the growth needs to be tested. The pension commencement lump sum (Tax Free Cash amount) should not be included. The amount put into drawdown in 2009 was £393,750, so the pension value has grown by £257,500. This will use up 25% of the LTA.

Only the growth in pensions originally crystallised post A-Day are caught by BCE 5A. Therefore, only two of Brian's three pensions will be tested on his 75th birthday.

The Results:

So even with only two of the pensions being tested Brian is going to exceed the LTA. Fortunately, Brian has not made a pension contribution since 2015 and is still eligible to apply for Fixed Protection 2016. This will give him available lifetime allowance of 50% of £1.25m (£625,000) rather than 50% of £1.03m (£515,500).

Looking again at the two pensions to be tested, the total value is £638,600: Brian will still be slightly over the LTA. If left as is, the excess £13,600 will be subject to a 25% LTA excess charge on his birthday. It would then also be subject to income tax when withdrawn from the pension.

Brian is normally a higher rate taxpayer, but he has been unwell for much of this year and has needed far less income from his pension than normal. He will be able to take a £13,600 income payment and only pay basic rate tax.

Withdrawing the money will mean that it can no longer benefit from the tax efficient investment growth a pension provides and would form part of Brian's estate for inheritance tax purposes if something were to happen to him. However, in this case he is likely to use the relatively modest amount for normal expenditure, and as he is likely to return to being a higher rate tax payer going forward, it is highly likely that taking an income payment and paying income tax will be the cheaper option for him.

Do not act on this information alone! Always seek independent financial advice before taking any action.

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