Is Flexi-Access Drawdown too good to be true?

For many years it has been possible to take benefits from a pension scheme in a method known as a pension drawdown. This approach has undergone various changes and until 2015 the most common form was “Capped Drawdown”.

In 2015 the government changed the rules (again). From ‘left field’ a new form of drawdown was introduced known as a Flexi-Access Drawdown. In short, a Flexi-Access Drawdown is similar to Capped Drawdown with a significant exception that there is no restriction on the income that can be withdrawn: there is no maximum or minimum.

This change in rules has resulted in an incredible opportunity for that lucky niche of people approaching retirement with cash available (personally or from a business) to make significant pension contributions.

Consider the following example:

- Mr Smith (age 65) is receiving his State and Occupational Pension and continues working on a consultancy basis. His total Pension Income is £30,000 p.a. and his Consultancy Income is £70,000 p.a.
- In each of tax years 2020/21 and 2021/22 he makes a gross personal pension contribution of £40,000, i.e. £80,000 in total. Net of tax relief at 40% his effective outlay is 2 x £24,000, i.e. £48,000.
- On 6th April 2022 Mr Smith converts his pension (which we assume has not changed in value & is purely these two pension contributions) to a Flexi-Access Drawdown.
- His initial Flexi-Access Drawdown fund is £80,000, from which he can take 25% as a tax free lump sum, i.e. £20,000.
- After taking the tax free cash the residual fund is £60,000. As he is in Flexi-Access Drawdown he can withdraw this residual fund as and when he wants.
- If £20,000 is drawn in each of the 3 tax years after his consultancy has finished and if we assume it is all taxed at 20%, the net Flexi-Access Drawdown income received will be £48,000 (i.e. £20,000 x 80% in each of the 3 years).
- Thus for a total net outlay of £48,000 he has received total net receipts of £68,000, i.e. £20,000 tax free cash plus £48,000 net Flexi-Access Drawdown, i.e. a profit of £20,000 (less fees and charges).

Of-course there could be reasons why Mr Smith might not want to make withdrawals from his pension fund, one being that the fund does not form part of his estate and is therefore not subject to Inheritance Tax (IHT) upon his death. If reducing IHT is not a priority though, then such an approach really does seem too good to be true.