What happens to my pension when I reach age 75?

Historically age 75 was an important milestone but this has now largely passed. It used to be a pension holder was required to purchase an annuity at this age, though is no longer the case.

At the time of writing there is no requirement to every buy an annuity, and whilst “no-one never needs to buy an annuity ever again” was proudly announced by the then Chancellor, George Osborne, in 2014, the truth is that compulsory annuitisation has not existed for some considerable time.

So currently at the age of 75 an individual can continue in drawdown, and the available income strategies from a pension is no different over 75 as would be under 75.

Lifetime Allowance Test

The relevance of 75 as a significant milestone is that many people we see the last ever test against the lifetime allowance at 75.

In the current tax year (2018/19) the lifetime allowance is £1.03 million and it is promised to increase with inflation in the future.

For those that have cumulative “crystallisation events” exceeding this lifetime limit, at 75 there can be a tax charge which typically will be either 25% and 55% depending on whether the individual chooses to leave the fund value in the pot or to draw it all down as a lump sum.

The method for calculating the lifetime allowance value and commensurate charge is complicated and outside the scope of this piece.

Tax Free Lump Sum

It used to be the case that any tax free lump sum that was not taken at 75 would be lost. This has not been the case in the legislation for many year.

However, this is not to say that existing contracts have been updated to reflect the legislation and therefore care must be taken approach this age. For many people age 75 is **not** the right time to take their tax free lump sum, which is contrary to the conventional wisdom.

The reason for this is the pension fund ordinarily grows free of income and capital gains tax and moreover the value of a pension is not part of the estate for inheritance tax. As there is not usually a lifetime allowance test beyond 75, the reasons an individual **under** the age of 75 should not take a lump sum are similar to those why it should not be taken by those **over** age 75.

Most of the time the lump sum available from a pension at 75 would be less than that which would be available at 80 or 85 so why not leave taking the lump sum until later?

For me, that the pension is ordinarily free of inheritance tax is significant. Often the intention, if the lump sum is taken, is not to spend it but to put into a bank account or ISA that is subject to inheritance tax, and possibly may be subject to other taxes, then the net position could indeed be worse for some people.

The major argument for taking the tax-free element is that lump sum death benefits (normally the fund value) from a pension are ordinarily tax free under 75 (ignoring the lifetime allowance), but there is the risk of tax beyond the age of 75. As long as existing pension contracts allow a pension fund can now be passed down to any recipient (or recipients) free of inheritance tax and other taxes as it is transferred – this is a valuable benefit. A pension fund passed down where the holder is over 75 would be taxed on the recipient as income as they drawdown, but with good planning these taxes will seldom be more than 20%, and could be as low as 0%. So whilst this could be inferior to the tax-free lump sum that could have been withdrawn immediately prior to death, that same lump sum might be hit by inheritance tax, and consideration needs to be given to this tax differential.

This is not to say that an individual will never take their tax free lump sum, but to assume it will always be taken at 75 is a gross oversimplification and will be to many people's detriment.

Summary

For most people age 75 is just another birthday!

For those at or above the lifetime allowance, or those that are likely to be above this level at 75 there is a definite planning need to mitigate lifetime allowance charges and ensure that they are in the appropriate pension investment vehicle at this age.

Taking the lump sum for many people at age 75 is the **wrong** decision, but thought needs to be given to the various factors that would make this decision more or less appealing – it rarely makes sense just to sit on the lump sum in a bank account after it is paid.

Finally whilst it has not been compulsory to purchase an annuity age 75 this is what the legislation allows, not true of all pension contracts, so it is worth making sure that your current providers allow you the full range of options and the benefit of the post-2015 rules when in advance of 75.

Pension planning, specifically lifetime allowance planning, is one of my core specialities, so if any of the above affects you, please get in touch.