

PREMIER PENSIONS MANGEMENT

LEGISLATION UPDATE : 5/05

Commutation of Trivial Pensions

As you are no doubt aware, the Government's plans for tax simplification will come into force with effect from 6 April 2006. The rules associated with commutation of trivial pensions will alter as part of these changes.

Current Regime

The current regime allows for the following:

- i. Subject to contracting-out requirements, any pension below £260 per annum can be trivially commuted at retirement (at any age after 50), regardless of the member's benefit entitlements in other arrangements.
- ii. Tax is payable at the rate of 20% on any part of the lump sum (excluding the value of spouse's benefits) that exceeds the Inland Revenue maximum tax-free lump sum.

New Regime

The new regime allows for the following (though this is still subject to possible amendments/changes before 6 April 2006):

- i. Trivial commutation is allowable between ages 60 and 75.
- ii. The total value of the members' benefits from all arrangements cannot exceed 1% of the Lifetime Allowance. At inception this will be £15,000, which translates to a pension of £750 per annum using the Revenue's 20:1 conversion factor.
- iii. A trivial commutation may only be paid within twelve months of the first time the member has trivially commuted benefits from any arrangement.
- iv. Trivial commutation lump sum will generally be taxed as a pension income, although the first 25% will be provided tax-free.

Effects of the Change

It is likely to become more difficult to commute small pensions, as total benefits from all arrangements cannot exceed 1% of the Lifetime Allowance and there is an increase in the minimum age from 50 to 60. In addition, there is currently no requirement to consider anything other than the benefit in your scheme. These requirements, and the fact that there is only a twelve month period for such lump sums to be paid, will increase administrative complexity for any cases that do proceed following the changes.

Possible Course of Action

The Trustees may wish to consider an exercise to commute as many small pensions as possible before 6 April 2006 (when the new regime comes into place) on the grounds of triviality.

As well as the issues discussed above, the administration of small pension benefits is relatively expensive to provide. Furthermore, the Pensions Protection Fund (PPF) is to be introduced in the near future and a significant part of the PPF levy will be membership based. Discharging benefits by trivial commutation will therefore reduce the scheme's levy payments.

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