

## **Triviality Rules & Case Study**

On A-Day (6 April 2006) the rules regarding trivial pensions changed. Individuals are now able to take (commute) the whole of their pension fund as a lump sum provided their benefits value falls within the triviality limit. This limit is 1% of the standard lifetime allowance (SLA) i.e. £16,000 for the 2007/08 tax year. This case study looks at a typical situation for a married couple Bob and Sarah who want to make the most of the new triviality rules.

Before we go into detail on the case study it's worth pointing out the main conditions which must be met in order to apply for triviality. These are:

- • no previous trivial lump sum paid more than 12 months ago
- • all of the benefits under the scheme have to be taken at the same time
- • the total benefits value of the individual's pension savings is not more than 1% of the SLA in force at that point
- • the member has some SLA available
- • the member is between ages 60 and 75
- • 25% of the lump sum will be tax-free, the balance will be taxed at the member's marginal rate.

### **Case study**

Sarah is 60 and married to Bob who is 62. Bob runs his own successful accountancy business where he employs Sarah on a part time basis as a receptionist/personal assistant. Bob earns around £60,000 a year and Sarah earns £15,000 a year. They've never really got round to sorting out their pension planning but have read a lot in the press about the pension changes that came into effect on A-Day. They both want to set up a pension and have around £20,000 between them to invest. They have approached their financial adviser to find out if there's anything that can be done to make the most of their £20,000 investment and plan for their retirement.

Their financial adviser explains that they could both make use of the new triviality rules from ADay (assuming that all the conditions above are met) and benefit from tax relief. Bob and Sarah both think that this sounds too good to be true and ask their financial adviser how this can be done. Their financial adviser explains that if they each invest £10,000 into a stakeholder plan now they will receive basic rate tax relief on their contributions. Bob's higher rate tax relief (the difference between basic and higher rate) will need to be claimed via his self-assessment tax return.

Provided each stakeholder plan does not have a benefits value of more than 1% of the SLA (£16,000 in 2007/2008 tax year), they will both be able to take (crystallise) their pension benefits as a lump sum (subject to tax).

**Triviality pursuit**  
**A-Day**

Their financial adviser does a few calculations for Bob and Sarah to illustrate how they could make the most of this opportunity assuming they each invest £10,000 into a stakeholder plan (no allowance has been made for any investment growth or charges under each plan):

	Bob	Bob	Sarah
Tax position	Higher rate	Higher rate to basic rate	Basic rate
Net payment	10,000	10,000	10,000
Grossed up at basic rate tax relief (22%)	2,821	2,821	2,821
Gross payment	12,821	12,821	12,821
Higher rate tax relief claimed via self assessment (18%)	2,308	2,308	n/a
Effective net payment	7,692	7,692	10,000
TFC (25% of benefits value of £12,821)	3,205	3,205	3,205
Balance of payment subject to tax (£12,821 - £3,205)	9,616	9,616	9,616
Less higher rate tax due (40%)	3,846	N/A	N/A
Less basic rate tax due (22%)	N/A	2116	2116
Net trivial commutation payment	5,770	7,500	7,500
Plus TFC	3,205	3,205	3,205
Total payment received	8,975	10,705	10,705

Looking at Sarah's position she will receive a clear £705 increase in her net payment in the table above. Bob's position is a little trickier – if he can change his tax position from a higher rate taxpayer to a basic rate taxpayer he will also receive a clear £3,013 increase in his net payment. However, if he remains a higher rate taxpayer he would receive £8,975 compared to his effective net payment of £7,692, an increase of £1,283.

In summing up their financial adviser explains:

- Bob and Sarah cannot use the triviality payment rules more than once.

- Each of their pension plans will require monitoring to ensure that they are not in danger of reaching the triviality limit.
- Both Bob and Sarah's tax status throughout the whole exercise is crucial if they want to make the most of this financial planning opportunity. For example, using Bob's figures in the table above his position clearly improves if his tax status changes from a higher rate taxpayer at outset to a basic rate taxpayer.
- They could both delay crystallising their benefits until a later date. This would allow them to take advantage of any increase in the triviality limit and also any investment growth achieved when they choose to crystallise their benefits.

This case study is an example only, and whilst it highlights some of the opportunities for planning, it should be recognised that it is not a complete or exhaustive description of the opportunities or pitfalls.

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