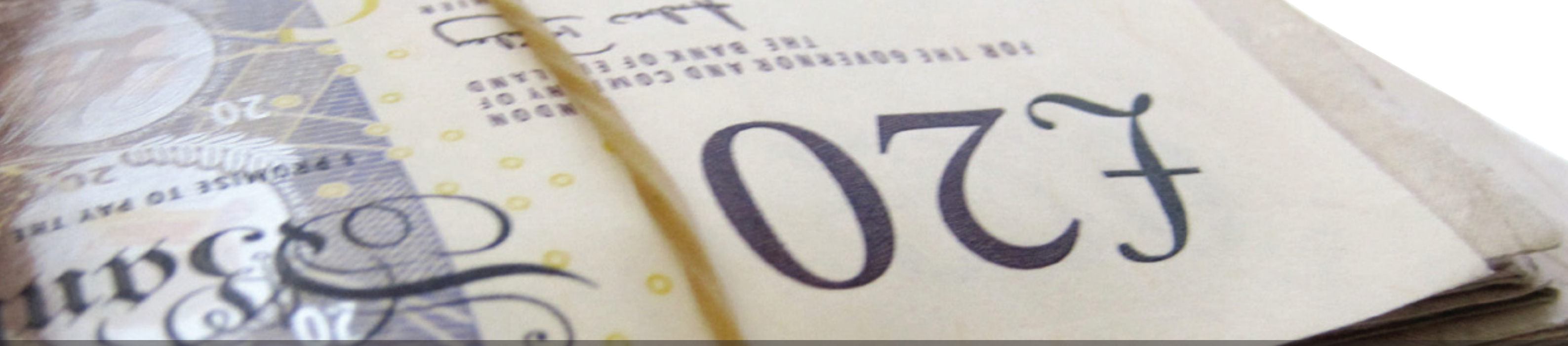

UK pension drawdown for US Citizens

by Andrea Solana of MASECO Private Wealth

Pension freedoms were introduced in April 2015 in the UK allowing individuals aged 55 and over with a UK defined contribution pension to be able to drawdown their pension however they wish (though there are tax consequences). As an American living in the UK, there are several considerations to think about when it comes to taking distributions from your UK pension.

Primary pension drawdown options

1) **Full lump sum distribution** - If you require greater liquidity or control over your finances in the short-term you could decide to take your entire pension pot in one lump sum, and invest/spend the funds as you wish, although taxation rules could significantly deplete your fund.

2) **Purchase an Annuity** – If you desire a more secure and regular income stream you can purchase an Annuity at retirement or a later chosen date. Annuities are insurance products that allows you to swap your pension pot for a guaranteed regular income which lasts for your lifetime or a specified period of time. Purchasing an Annuity is an irreversible decision.

3) **Flexi-access drawdown** – This option allows you to draw down different amounts over any period of time. It can be considered if you would prefer to keep your assets invested in the tax efficient wrapper for as long as possible and wish to access the funds over time. The amount of distribution can vary and the tax paid on the distribution will be determined by tax residency and amount of distribution.

4) **Uncrystallised funds pension lump sum (UFPLS)** – This allows you to withdraw a single or series of lump sums from your pension without the need to move the funds into a drawdown product first. It can be considered if you would prefer to keep your assets invested in the tax efficient wrapper for as long as possible and wish to access the funds over time. If the entire pension fund is not withdrawn at once, then 25% of each lump sum may be taken tax-free with the balance taxed at your marginal rate of income tax. Not all pensions offer this flexibility so it is possible that you may need to transfer to a more flexible arrangement.

Individuals generally have the ability to choose one distribution option for their entire pension fund or choose different distribution options for segments of their pension fund. Up to 25% of the pension fund is generally available to be taken tax-free from a UK perspective.

Which strategy is right for you?

The ability to choose flexible drawdown over an Annuity offers increased control and flexibility on the use of your pension assets. However, this option also bears some risk as it is no longer a secure Annuity and requires careful management to ensure you do not unknowingly deplete the account through excessive income drawdown.

In order to begin assessing which distribution strategy is right for you, you need to have a good understanding of your financial goals and objectives as well as your income needs from your pension and other assets. Give some thought to some of the questions outlined below which help to frame your financial goals for the money:

★ What does retirement mean to you? Will you stop work altogether or will you continue to earn a partial income stream?

★ What lifestyle do you want in retirement? Regular holidays? How much income will you need your assets to generate and will that income be needed regularly or at reaching certain milestones?

★ Where do you want to live in retirement? In the UK, the US, or somewhere else?

★ How much risk can you afford to take with your income? How much risk do you feel comfortable with? Will short-term volatility affect your ability to meet your everyday needs?

★ Do you feel comfortable in retaining an ongoing involvement in managing your retirement income?

★ Will family members be reliant on monies from your pension when you die?

★ Do you want to leave an inheritance to a specified individual? If so, do you have assets that you can draw upon before using your UK pension savings?

Considerations for a US person

Pension flexibility freedoms help provide opportunities to US individuals to liquidate their pensions in a tax-efficient manner that also makes sense for their individual situation. Individuals no longer potentially face liquidity restrictions if accessing a large lump sum is a suitable drawdown strategy.

Distributions from a UK pension can be treated differently for tax purposes depending on the type of distribution, the tax residency of the pension owner and the application of the US-UK tax treaty. Generally, when it comes to periodic pension distributions, the primary taxing rights lie with the country of residence, not where the pension is located. What this means is that if a US citizen who is UK resident begins taking periodic distributions from their UK pension, the UK will have primary taxing rights on the distribution. Despite this, the US will often require US citizens to report UK pension distributions in the US as well with UK foreign tax credits generally available to offset any US tax payable.

There are now many planning opportunities for Americans as they approach retirement and decide where their retirement years will be spent. The best place to allocate your pension dollars and the amount you should ultimately seek to contribute to a pension, as well as your planned drawdown strategy in the future, should become a planning focus and point of discussion with your tax adviser as well as your wealth manager. ★

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