



Legislative change to tax code

Tax code used on 'trivial commutation' and similar lump sum pension payments

PAYE tax code change

From April 2013 - a change in the tax code applied to “trivial commutation” and similar one-off lump sum pension payments from registered pension schemes.

Under pension tax rules, for registered pension schemes, pension payers are able to convert certain small pensions into a one-off cash payment. Subject to certain conditions, a maximum of 25% of the value of most of these small pensions can be converted to a tax free lump sum. The tax code is then applied to the remaining taxable portion of the lump sum.

Currently, pension payers are required to operate the emergency tax code (code 810L for 2012-13) on the non-cumulative (week 1 / month 1) basis on the lump sum pension payment. Applying the emergency code in this way results in many lump sum payments of this type attracting the higher, and possibly additional, rates of tax. And in many cases this leaves the payment recipient in a position where they temporarily overpay tax.

From 6 April 2013, it is proposed that the basic rate (BR) tax code (operated on the non-cumulative basis) will apply. We believe this change will result in more individuals, in particular those on low to moderate incomes, paying the right amount of tax at the time the lump sum pension payment is made.

Trivial commutation and similar one-off lump sum pension payments include:

- trivial commutation lump sums¹,
- trivial commutation lump sum death benefits²,
- winding up lump sums³,
- winding up lump sum death benefits⁴,
- commuted equivalent pension benefits⁵,
- certain small lump sum payments⁶ and
- ‘small pot’ commutations⁷.

Draft legislation and a technical note relating to PAYE and Real Time Information changes, including this proposed change, will be made available for comment on the HMRC website for a period of eight weeks from mid-November 2012.

Note: The P53 form and process, used to claim any overpaid tax, will continue to exist in its present form. However, HMRC are currently working with representative bodies to improve both the form and process for individuals, pension payers and HMRC.

¹ under paragraph 7 or 7A of Schedule 29 Finance Act 2004

² under paragraph 20 of Schedule 29 Finance Act 2004

³ under paragraph 10 of Schedule 29 Finance Act 2004

⁴ under paragraph 21 of Schedule 29 Finance Act 2004

⁵ under regulation 2(a) of the Registered Pension schemes (Authorised Payments) Regulations 2006 [SI 2006/209]

⁶ under regulations 6, 8 and 10 of The Registered Pension Schemes (Authorised Payments) Regulations 2009 [SI 2009/1171]

⁷ under regulations 11, 11A and 12 of The Registered Pension Schemes (Authorised Payments) Regulations 2009 [SI 2009/1171]