Pensions Newsletter

March 2014

Budget Special

George Osborne's budget has introduced the most radical reforms on the current pension system in the UK for a generation. Below is a summary of these changes and what they might mean for you:

The current situation

Under current legislation, anyone wishing to draw income from their defined contribution pension fund must either purchase an annuity (which is a regular income payable for the rest of your life) or else use Income Drawdown. With Income Drawdown, the fund continues to be invested and you can withdraw certain levels of income from the pension capital. Income Drawdown provides greater flexibility but there are still restrictions on how this income can be taken. In effect there are two different types of Income Drawdown:

- Capped – with Capped Income Drawdown there are limits on the maximum amount that can be taken from your pension fund of 120% of the Government Actuary Department (GAD) rates. These are effectively age-related tables published by the Government.
- Flexible – with Flexible Income Drawdown there are no limits as to the income that is withdrawn from the fund (hence the whole fund can be taken in one go, if desired). However, in order to qualify for Flexible Income Drawdown you must have secured alternative pension income from other sources (which can include the State benefits) of at least £20,000 per annum.

When you come to take your benefits 25% of the fund can be taken as a tax free lump sum. Any income taken from your pension is taxable as income (i.e. at either a rate of 20%, 40% or 45% depending on how much income you have from all sources).

Anyone who is at least aged 60, who only has a "small" pension fund can potentially withdraw the whole fund as a lump sum. This can be used if the total value of all your pension funds is less than £18,000. Alternatively, any small pots with a value of £2,000 or less can be taken as a lump sum regardless of the value of your pension funds held elsewhere. A maximum of two personal pension or stakeholder pensions (which will include group arrangements) can be commuted in this way. There is no restriction on the number of occupational pension pots that can be taken in this way.

The first 25% of any funds taken in this way will be tax free with the remainder subject to income tax.

The changes

With effect from April 2015 anyone aged over 55 will be able to take their whole defined contribution pension pot as a lump sum regardless of the level of income (pension or otherwise) they have elsewhere. As at present, 25% of this will be tax free. The remainder will be taxed as income.

This means that with effect from April 2015, there will no longer be a requirement to purchase an annuity with your pension pot. This is obviously very good news for pension savers as for some years now annuities have been viewed as poor value for money. These changes give greater flexibility and greater control to pension savers as to how they take their pension income.

Anyone wishing to take the whole of their pension fund as a lump sum should bear in mind that 75% of the fund taken in this way will be subject to income tax. As income tax rates are based on total income during the tax year, for many people taking income in this way will mean that they may suffer a higher rate of income tax than they would usually pay. For example, those usually subject to basic rate tax (20%) may find they are subject to higher rate tax (40%) or those who usually pay higher rate tax (40%) may find that they pay tax at the additional rate (45%). Under the current system anyone wishing to withdraw the whole fund as a lump sum at retirement will face a tax charge of 55%. The new system will therefore represent a reduction in the tax rate paid for anyone wishing to withdraw the fund in this way.

As these changes are not due to come in until April 2015 interim measures have been introduced which will apply from 27th March 2014. These measures are as follows:

- The level of alternative pension income required in order to use flexible drawdown will decrease from £20,000 to £12,000.
- The limits on capped income drawdown will increase from 120% to 150% of the GAD rates.
- The limit on “pot size” for taking all your pensions as a lump sum will increase from £18,000 to £30,000.
- Individual pots of less than £10,000 (increased from £2,000) can also be taken as a lump sum regardless of the value of any other pension arrangements. Again this will apply to any occupational pension pots plus up to two personal pensions or stakeholder pension pots.

The budget also announced that every person will be given the right to “free, face-to-face, impartial advice” when they come to retirement in order to help them make the right choices. A £20 million development fund will be provided over the next two years in order to help establish this service. How this will work in practice remains to be seen.

Other Budget news . . .

ISAs

At the moment there are two different types of ISA; a cash ISA and a stocks and shares ISA. There is an overall limit that can be paid into an ISA of £11,520 of which a maximum of £5,760 can be paid into a cash ISA.

The plans are to create a single New ISA (NISA) which will be able to contain both stocks and shares and cash. The total threshold on the amount that can be placed into a NISA will increase to £15,000 per annum.

Personal Allowance

The Personal Allowance is the amount of income an individual can earn each year without paying any tax and this will increase from £9,440 to £10,000 with effect from 6th April 2014. This will increase to £10,500 with effect from 6th April 2015.

This summary is based on One Pension Consultancy's understanding of the budget on 19th March 2014. It is not intended to provide advice nor does it look at the options in retirement in any detail. Anyone requiring further information on the options at retirement can request a copy of One Pension Consultancy's *Guide to Retirement*.

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