Pensions Flexibility Update March 2015

Removal of the limit on the level of pension that can be drawn from 6th April 2015

In his March 2014 Budget, the Chancellor George Osborne announced sweeping changes that will remove the limits on the pension benefits that can be drawn from your pension scheme each year as well as reduce the taxation of benefits payable to your family in the event of your death.

The Taxation of Pensions Act 2014 has now confirmed the details of those proposals and the new rules will come into force on the 6th April 2015. This pension bulletin gives you an update on the new rules and how they might affect you.

We are currently developing the necessary literature and forms to ensure that the full range of options will be available to our clients on the 6th April 2015. We will be updating our website http://www.dapco.co.uk with our progress and forms as they become available.

Your Pension Options

Under current rules, you can usually take your pension benefits from age 55. This age restriction is not changing and so the options outlined in this bulletin will only be available to members once they reach that age.

When you crystallise your benefits you are usually entitled to take 25% of your fund as a tax free lump sum (the pension commencement lump sum or PCLS). In addition to the PCLS, you can take a pension which is taxed as earned income. The new rules change the pension options that are available to you.

Flexi Access Drawdown (FAD)

FAD will allow you to take any level of income from your drawdown fund with no annual restrictions. You can take regular payments or one off ones, and vary the amounts at any time. This means that you can take your entire pension in one go or over time. However, it may not be tax efficient or sustainable to do so. If you are reliant on your pension to support you, you may need to consider taking a lower level of income which can sustain you for the rest of your life. Taking an income from a FAD fund will trigger the new money purchase annual allowance rules (outlined later in this Update).

Uncrystallised Funds Pension Lump Sum (UFPLS)

UFPLS will be an alternative way to access your pension benefits from funds not already in drawdown. It allows you take a one off payment or a series of payments while keeping the remainder of your pension uncrystallised.

When you take a UFPLS payment, 25% of the payment will be tax free and 75% of the payment will be taxed as pension income at your marginal rate of income tax.

Payment of a UFPLS will be a benefit crystallisation event and we are required to test your fund against the lifetime allowance, which is currently £1.25 million. There may be tax consequences where the total of all payments and previous crystallisations exceed the lifetime allowance.

The UFPLS is not available on funds that are already in drawdown. Payment of a UFPLS will not be available to members if they have rights to a disqualifying pension credit, primary protection, enhanced protection or a right to take a tax free lump sum of greater than £375,000 on 5th April 2006.

Access to impartial guidance – Pension Wise

In addition to the sweeping changes in his Budget, the Chancellor also announced that everyone should have access to free impartial guidance to help them make sense of their options.

This guidance will be provided through a new government service called Pension Wise. The Pension Wise service can be accessed online, over the phone with the Pensions Advisory Service and face to face at the Citizens Advice Bureau. The Pension Wise website can be found at www.pensionwise.gov.uk. We understand that the full service will launch on 6th April 2015, but you can visit the site now and register your interest to get early access to the service.

Please note that, while this service will provide useful information, it is not intended to be a substitute for full financial advice from a regulated financial adviser.

Changes to Contribution Levels

Money Purchase Annual Allowance Rules (MPAA)

The annual allowance is the total amount that can be contributed to a pension scheme each year and will qualify for tax relief. The standard annual allowance is currently £40,000.

However, flexibly accessing your pension savings will trigger the money purchase annual allowance (MPAA) rules which will reduce your annual allowance from £40,000 to £10,000 per annum for money purchase savings (special rules apply to 'final salary' schemes). This will be effective from the day after the trigger event occurred. The MPAA rules also prohibit the ability to carry forward any unused annual allowance.

The following actions will trigger the money purchase annual allowance rules as you will have flexibly accessed your pension savings; taking an income under Flexi Access Drawdown; taking an Uncrystallised Pension Lump Sum; taking a stand alone lump sum with Primary Protection; taking income under a flexible annuity.

If you flexibly access your pension savings we will issue you with a Flexible Access Notification which will explain the reason for the notification being issued along with confirmation of any actions you will need to take.

What if you have already taken benefits from your pension?

If you have already taken benefits from your pension and you are in income drawdown (either capped drawdown or flexible drawdown) then you will be able to benefit from the new rules. If you are in scheme pension, or are receiving your pension income through an annuity then you will not be affected by the new rules.

Capped Drawdown

Capped drawdown is a current drawdown option which allows you to take an income from your pension fund limited to a maximum annual amount, which we calculate on a regular basis. Under the new rules, capped drawdown will not be available if you take your benefits for the first time from the 6th April 2015 onwards. However, if you are already in capped drawdown then you have a couple of options.

If you do nothing then you will continue in capped drawdown. We will continue to calculate your maximum annual pension amount just like we currently do. If you stay in capped drawdown then you will not be subject to the money purchase annual allowance rules, meaning that your annual allowance will remain at £40,000. In order to remain in capped drawdown you must not exceed your maximum annual pension amount.

If you had crystallised part of your fund rather than the whole fund, then you will also be able to designate new funds into your capped drawdown fund without triggering the money purchase annual allowance rules.

If you would like to take advantage of the new flexible options then you can convert your fund into a Flexi Access Drawdown (FAD) fund at any time. You can do this by completing our Flexible Access Member Declaration Form. Converting your capped drawdown fund into a FAD fund will remove the annual income limit on your pension, but it will also trigger the money purchase annual allowance rules, meaning that your annual allowance will reduce to £10,000.

Flexible Drawdown

Flexible drawdown is a current drawdown option which allows you to draw any level of income without limits provided you meet certain requirements. One of those requirements is that you cannot pay any further contributions to your pension funds.

Flexible drawdown will cease to be available to members from the 6th April 2015. If you are currently in flexible drawdown then we will automatically convert your fund to a Flexi Access Drawdown fund on the 6th April. The money purchase annual allowance rules will apply, meaning that your pensions will be able to receive contributions, but you will be limited to £10,000 per annum.

Changes to Death Benefits

Changes to how death benefits can be paid have also been introduced to be effective for payments made from 6th April 2015. You may like to review your death benefit nomination in light of these new options.

The Current Rules

You can nominate anyone you would like to receive your death benefits. If you die under the age of 75 and before drawing any benefits then your nominated beneficiaries can usually take your fund as a tax free lump sum outside of your estate. Once you have reached age 75 or taken your benefits then the lump sum becomes taxed at 55%, or dependants could take an income from your fund subject to income tax.

The New Rules

Under the new rules, you can continue to nominate anyone that you want to receive your death benefits. Your nominated beneficiaries can choose to take their benefits as a lump sum or as an income under the new flexi-access drawdown rules.

The tax treatment of these payments will depend on your age when you die (pre or post age 75) and whether the funds are designated and/or paid to your beneficiary within 2 years. Designating the funds just means that they are moved into the beneficiary's name, it doesn't mean that any payments have to be made.

If you die before you reach age 75 and your funds are paid to your beneficiaries within 2 years then the payments will be tax free, irrespective of whether you had taken any benefits or whether the beneficiary take them as a lump sum or as flexi-access income.

If you die after your have reached age 75, then the payments will be subject to a tax charge, which is normally the beneficiary's marginal rate of income tax, but will be 45% if taken as a lump sum in the 2015/16 tax year.

What happens when a beneficiary dies?

If a beneficiary dies, having not drawn out the entire fund, then the funds can be passed on again. The beneficiary can nominate successors, who will have the option of taking the funds as a lump sum or as flexi-access income.

The tax treatment of these payments will depend on the age of the beneficiary when they die (not on your age when you died). There is no limit to the number of times the funds can be passed on to successors. So provided it is not all taken out, your pension could be passed on for generations.

About this document

This Update is based on our understanding of the legislation recently published by HMRC with regards to pension flexibility for money purchase schemes from 06 April 2015.

Every care has been taken to ensure that it is correct. It is issued by D A Phillips & Co Ltd for use by our SSAS clients and their advisers.

Please note that D A Phillips & Co Ltd is not authorised to give financial advice. We do not know all of your circumstances or details of any other pension schemes of which you are a member. You should contact your financial adviser for help on how this legislation may affect you personally.

No responsibility to any third party is accepted if this information is used for any other purpose. The legislation and HMRC practice may change in the future.

If you have any queries regarding the information in this Bulletin and how it affects your circumstances then please contact your financial adviser.

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