



NEWSLETTER Summer 2010

COALITION GOVERNMENT ANNOUNCES A MAJOR REVIEW OF PENSION BENEFITS AND RELIEFS

Following the announcement in the Emergency Budget that the age 75 'threshold' would be raised to 77, pending a thorough review of the existing drawdown rules, both before and after reaching age 75, the Treasury has now published a consultation paper on the subject, with the intention that the changes take effect from 6 April 2011.

A second consultation paper has been published regarding the Annual Allowance, the Lifetime Allowance and tax relief on pension contributions.

PROPOSED CHANGES TO UNSECURED PENSION RULES

The key proposals are:-

1. No formal requirement to take pension benefits at any age, although a tax-free cash lump sum will only be available if the scheme member is under 75.
2. Alternatively Secured Pension ("ASP") to be abolished, with effect from 6 April 2011, after which all funds in drawdown will be classed as Unsecured Pension ("USP"), regardless of age.
3. From the member's 75th birthday all pension funds are deemed to be in USP, even if no benefits have been taken.
4. Part of the USP fund will be classed as "**capped drawdown**" and will operate in a similar manner to current USP, although new limits may be introduced.
5. "**Flexible drawdown**" will be allowed where individuals can demonstrate that they have satisfied the "**Minimum Income Requirement**" ("MIR"). Up to the whole amount of the fund qualifying for Flexible Drawdown may be withdrawn, subject to income tax at the member's marginal rate.
6. All lump-sum death benefits paid from a fund in USP will be taxed at 55%, irrespective of age.

Transitional Arrangements

The current rates of taxation on death benefit lump sums paid from pension funds in drawdown will remain as they are for any member who dies prior to 6 April 2011, subject only to the transitional arrangements announced in this summer's emergency Budget, i.e.:-

- 35% in USP (i.e. under age 75 as at 22 June 2010)
- Up to 82% in ASP (i.e. 75 or over as at 22 June 2010)

Minimum Income Requirement

The proposals do not specify the proposed level of MIR but it will include the various state pensions and secured pension income increasing by at least Limited Price Indexation (so for example level annuities would not qualify).

The impact of the new rules will depend very much on how high the MIR is set.



PROPOSED CHANGES TO ALLOWANCES AND TAX RELIEF

Annual Allowance

The Government is looking at reducing the Annual Allowance to £30,000-£45,000 as a replacement for the over-complex 'Anti-Forestalling' measures introduced by Labour. The likely level of Annual Allowance is £40,000, which figure may be indexed.

Lifetime Allowance

The Government is looking at the possibility of reducing the Lifetime Allowance to say £1.5 million (it is currently £1.8 million). It is also looking at freezing the value of rights covered by primary and enhanced protection. At this stage there is no indication of how such measures would work.

Tax relief

The consultation proposes capping tax relief at 40% on contributions below the (new) annual allowance, even for 50% taxpayers.

PRACTICAL IMPLICATIONS

For most people with substantial pension funds and/or earnings subject to higher rates of tax the position will be one of 'wait and see'. However, as there is no proposal to change the availability of 25% tax-free cash on retirement, pension contributions remain tax-efficient for higher-rate taxpayers, especially those earning over £100,000 (because of the tapering of personal allowances and the introduction of the 50% tax band for those earning over £150,000). Individuals caught by the anti-forestalling measures should if possible look to use up at least their £20,000 Special Annual Allowance for the current tax year.

The only category that might decide to exercise caution is pension fund members with funds worth close to £1.5 million or more.

With regard to the taxation of death benefits the 'at risk' group is now limited to those individuals who were 75 before 22 June 2010 and have yet to secure their benefits. They will, however, join the rest of the population on 6 April 2011, as long as they survive that long. If this is in doubt, a scheme pension with a 10-year guarantee should be considered. Scheme pensions may still be attractive in some circumstances going forward (and not necessarily only for over-75's).

The views and opinions expressed in this document are based on Organon's interpretation of law and HMRC regulations at the date of publication and do not constitute advice. Individual pension fund members should obtain advice from a suitably qualified and authorised financial adviser. Please contact us if you would like further information on any of the issues raised:

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