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Update

Summer Budget 2015

In this issue:

- Tax relief changes.
- Pension Input Periods.
- Reduction in the Lifetime Allowance.
- Minor death benefit change.
- Delay to annuities in payment changes.
- Green Paper on overhauling the pension system.

Earlier this month the Chancellor delivered the first conservative Budget for 18 years. Various announcements were made which affect UK registered pension schemes. A summary of the main changes is as follows:-

Tax relief on pension contributions for 'high earners'

At present, the Annual Allowance for tax relievable pension contributions is £40,000 p.a.. Individuals also have the ability to carry forward unused allowances from the previous three tax years in certain circumstances.

The Chancellor announced that from 6 April 2016, anyone with an 'income' in excess of £150,000 will have their Annual Allowance reduced. This reduction will be tapered from £40,000 down to £10,000, with every £2 of income over £150,000 leading to a reduction in Annual Allowance of £1. Therefore, anyone with an income of £210,000 or above will have an Annual Allowance of £10,000. Furthermore, individuals will only be able to carry forward the tapered Annual Allowance to future tax years if this is unused.

The definition of income to be used is quite wide ranging and is expected to include salary, bonuses, rental income, salary sacrifice pension contributions, employer pension contributions etc. We will have to wait and see the makeup of the final legislation, but anyone with expected income within the above range will find it quite difficult to pinpoint the exact limit on their tax relievable contributions during the tax year in question.

Changes to Pension Input Periods (PIPs)

In light of the above proposals, the Chancellor has announced immediate changes to the Pension Input Period rules affecting all individuals. A PIP is the period over which a member's contributions are valued in order to test them against the Annual Allowance. In most cases, a member's PIP is aligned to the tax year, but this is not always the case. The changes that have been announced to the PIP rules are as follows:-

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- Any PIPs active on 8 July 2015 will cease on that date.
- A new PIP commences on 9 July 2015 and will cease on 5 April 2016.
- Transitional rules will apply for contributions made on or prior to 8 July 2015, giving individuals an Annual Allowance of £80,000 (plus the usual carry forward rules).
- The Annual Allowance from 9 July 2015 to 5 April 2016 will be £0, but up to £40,000 of the unused Annual Allowance from the period up to 8 July 2015 can be added to this (plus the usual carry forward rules).
- Future PIP's will be aligned to the tax years and individuals will no longer be able to alter their PIP.

All in all, these changes are quite complicated for the 2015/2016 tax year, but are simplified thereafter. Please contact your usual consultant if you or your scheme members need any assistance in working out the maximum allowable tax relievable contributions for the 2015/2016 tax year in light of the above changes.

'It's deeply disappointing to see politicians once again syphoning cash from tomorrow's pensioners to pay the bill for today's political priorities. Ensuring a decent deal for today's savers and tomorrow's pensioners will only come from a stable pension system on which people can depend not to change overnight. Pension saving shouldn't be treated as a secret ATM for Government finances.'

Joanne Segars
National Association of Pension Funds (NAPF)

Reduction in the Lifetime Allowance from 6 April 2016

As announced previously, the Lifetime Allowance will reduce from £1.25m to £1m from 6 April 2016. Protection will be offered for individuals who feel they will be affected by this reduction and we will be writing to clients separately on this issue as and when the protection regime is announced.

The Lifetime Allowance should increase in line with CPI from April 2018.

Changes to the taxation of lump sum death benefits

The benefits that can be paid on the death of a member altered from 6 April 2015. These changes were covered in previous newsletters. Any lump sums payable in respect of a member who passed away after the age of 75 are currently taxed at 45% for the 2015/2016 tax year. The Government previously indicated that from 6 April 2016 the tax rate would change to the recipient's marginal rate and this change has now been confirmed. Any payments made to non-individuals (such as a company or a trust) will continue to be taxed at 45%. Lump sums payable in respect of members who pass away prior to age 75 continue to be paid tax-free, provided the payment is made within two years of the date of death and subject to the usual Lifetime Allowance rules.

Delay in changes to annuities in payment

The Chancellor previously announced that from April 2016 members who have already purchase an annuity will be able to sell these contracts on a secondary annuity market. This would presumably then allow the member to flexibly access the current capital value of the annuity. However, these plans have been put back to April 2017.

It should be noted that any decision to cash in an annuity contract (if the rules go ahead) should not be made lightly. It is likely that this secondary annuity market will be relatively small and it is doubtful that this will offer value for money to individuals.

Consultation on pension tax relief

Probably the most significant announcement in the Chancellors Budget was that of a Green Paper on the future of the pensions industry. The Government are asking if the current 'exempt-exempt-taxed' operation of the pension system is the best mode of operation. They are seeking opinion whether an alternative 'taxed-exempt-exempt' system would be clearer to understand and would be a greater incentive for savers.

The current system operates by tax relief being given on contributions paid into a registered pension scheme (exempt). The majority of the growth within the fund is tax-free (exempt). The benefits payable on retirement are taxed (taxed) except for the tax-free retirement lump sum.

'If people are to take responsibility for their retirement, it is important that the support on offer from the Government is simple and transparent, and that complexity does not undermine the incentive for individuals to save.'

George Osborne

The Government are asking if an alternative system might be better. Paying contributions from taxed income with no tax relief granted (taxed), growth within the fund tax-free (exempt), then benefits payable on retirement would also be paid tax-free (exempt). This is essentially the way the ISA regime operates.

The consultation ends on 30th September and anyone is free to respond to the consultation. It remains to be seen what changes (if any) will be made as a result of this consultation. We expect the Government are hoping that a move over to a similar system to ISA's will attract more pension savings. However, overall it is likely that pension savers would lose out on a change of this nature, as the current tax relief granted on contributions would generally out-weigh the taxable benefits paid from pension funds under the current system. Furthermore, as the current system allows a tax-free lump sum to be paid, a certain portion of the current system operates on an exempt-exempt-exempt basis, and this would be lost altogether.

Please do not hesitate to contact your usual consultant at Hanover if you wish to discuss any of the above points in more depth.

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