

# Understanding the evolving landscape of UK pensions (March 2015)

## Summary of new retirement freedoms

You may have read about changes to how you can draw an income from your pension from 6 April 2015. This document aims to summarise what the legislation could mean to you if you are at or approaching the minimum retirement age which is currently 55 (but is likely to increase from 2028). The new flexibility is not available to defined benefit pensions.

## Retirement income on or after 6 April 2015

There will be three primary options for you to consider in terms of taking benefits for the first time on or after 6 April 2015. If you are not in capped drawdown prior to 6 April 2015 it will not be an option to move into capped drawdown after this date. Capped drawdown is the current form of drawdown that allows you to draw an income from your pension subject to an annual limit. Please see overleaf for more detail on how the annual allowance will operate from 6 April 2015 if you are in capped drawdown.

### Flexi-access drawdown

- This new form of income drawdown allows you take pension income (taxable) with no upper limit. You can take tax free cash (also referred to as pension commencement lump sum) with the remainder paid as income over a period of time or in one payment. This option is available to all individuals of minimum pension age.
- Flexi-access drawdown will replace capped drawdown for individuals setting up a drawdown plan for the first time on or after 6th April 2015.
- You can usually take a tax free lump sum but if you begin to take any income in addition to your lump sum, your annual allowance (value of contributions that you can pay to your defined contribution/personal pension plans and receive tax relief on) falls to £10,000. If you only take your tax free lump sum your annual allowance remains at the current annual allowance of £40,000.

### Uncrystallised funds pension lump sum (UFPLS)

- A lump sum can be taken from uncrystallised pension savings with this new option. Uncrystallised means that this portion of your pension has not had any tax free cash taken and/or it is not providing you an income. Typically, 25% of the lump sum will be tax free with the remainder being subject to income tax. For example you could take a £10,000 lump sum from your pension with £2,500 being paid tax free and the remaining £7,500 being paid as income but subject to tax.
- This option leaves remaining monies in your pension uncrystallised.
- Taking any UFPLS will result in your annual allowance being reduced to £10,000.

### Lifetime Annuities

- Payments from lifetime annuities can decrease as well as increase
- 10 year restriction on guarantees removed. Annuity provider can pay out for any period after the member's death provided it is clearly covered in the annuity contract. This means the annuity could continue pay income to the individual's estate for any defined period.

## What happens to my pension if I am currently in capped drawdown or move into capped drawdown prior to 5 April 2015?

If you are currently taking an income from your pension in the form of capped drawdown the following applies from 6 April 2015:

- You will continue in capped drawdown as long as the income you take does not breach your stated maximum.
- Your maximum income will continue to be recalculated every 3 years until age 75 and annually thereafter.
- As long as the income you take does not breach your maximum annual limit, your annual allowance remains at the standard annual allowance, currently £40,000 (2015/16).
- If you ever decide to take more income than stated under capped drawdown you will move into flexi-access drawdown. At this point your annual allowance reduces to £10,000.

## What happens to my pension if I am currently in flexible drawdown on or before 5 April 2015?

If you are currently taking an income from your pension in the form of flexible drawdown the following applies from 6 April 2015:

- Flexible drawdown will automatically convert to flexi-access drawdown.
- Annual allowance will be £10,000. Currently flexible drawdown customers have no annual allowance. Please note if you have a form of protection from reductions in the Lifetime Allowance you could lose this valuable protection by making a pension contribution.

## Can you explain how the annual allowance will work from 6 April 2015?

- If you are in capped drawdown your annual allowance will remain at £40,000 unless you ever decide to take an income above your maximum.
- Remember your annual allowance can only be up to 100% of your earnings and capped at the annual allowance amount which from 2015/16 will be either £40,000 or £10,000. If you are a non earner you can only pay up to £3,600 each tax year (£2,880 which is topped up with tax relief to £3,600).
- The money purchase annual allowance of £10,000 is triggered by being in flexi-access drawdown and drawing an income or a UFPLS has been paid.

- You may be able to continue to accrue benefits in a defined benefit/final salary scheme, up to a total of £40,000 every year, as the money purchase annual allowance only applies to defined contribution/money purchase pension schemes.
- There is no carry forward facility of the £10,000 money purchase annual allowance.
- In the first tax year/pension input period that the £10,000 money purchase annual allowance applies to any contributions paid to a defined contribution/money purchase scheme prior to the reduced annual allowance being triggered will not result in a tax charge. However, any subsequent contributions made after the date that the money purchase annual allowance is triggered could result in tax charge.

## What happens if I am already receiving income from an annuity?

If you are already receiving an income from an annuity you currently cannot change the income you receive. This may change in the future. If you have uncrystallised monies in a pension you can purchase a further annuity on or after 6 April 2015 and benefit from the new flexibility that annuities can offer or consider UFPLS or flexi-access drawdown.

## From next April can I genuinely withdraw all of my money from my pension?

Yes you can but please remember any payment of income (after your tax free lump sum) will be subject to tax at your marginal rate(s) of income tax. Therefore a more gradual approach to withdrawing an income may be more tax efficient dependent on your personal circumstances.

## Changes to Death Benefits

Currently, it is only possible to pass a pension on as a tax-free lump sum if you die before age 75 and have not taken any tax free cash or income from your pension. If you have taken tax free cash/income the pension is subject to a 55% tax charge. This has been a common reason in the past for clients purchasing an annuity.

From April 2015, you will be able to pass on your pension (defined contribution pensions only) to your beneficiaries tax free, (a two year rule applies) provided they keep the money in a pension. Should the beneficiary decide to make any withdrawals, they only have to pay income tax at their highest marginal rate if the original client dies after age 75.

## What happens to my pension if I die before age 75?

	Old rules (pre 6 April 2015)	New rules (from 6 April 2015)
<b>Lump sum</b>	Tax free if uncrystallised or 55% tax if in drawdown	Tax free if paid out within 2 years
<b>Income</b>	<ul style="list-style-type: none"> <li>• Taxed as income (via an annuity or drawdown)</li> <li>• Option available only to dependants</li> </ul>	<ul style="list-style-type: none"> <li>• Tax free if taken via income drawdown or an annuity if designated within 2 years</li> <li>• Option available to any beneficiary</li> </ul>

## What happens to my pension if I die after age 75?

	Old rules (pre 6 April 2015)	New rules (from 6 April 2015)
<b>Lump sum</b>	Subject to 55% tax	<ul style="list-style-type: none"><li>• Subject to 45% tax (unless paid as income) for payments made between 6 April 2015 and 6 April 2016.</li><li>• Taxed as income (at the beneficiary's/ beneficiaries' rate of income tax) on payments after 6 April 2016 subject to legislation being passed.</li></ul>
<b>Income</b>	<ul style="list-style-type: none"><li>• Taxed as income</li><li>• Option available only to dependants</li></ul>	<ul style="list-style-type: none"><li>• Taxed as income</li><li>• Option available to any beneficiary</li></ul>

### Very Important

When a client dies usually the Scheme Administrator has 2 years to pay a lump sum. If a payment is made after 2 years as a lump sum prior to age 75 a 45% tax charge will apply. If not designated to drawdown within 2 years prior to age 75 then any income is subject to income tax.

Its not unauthorised if made after 2 years but if paid as a lump sum (on deaths pre 75) then after 2 years 45% will be applied or if not designated in 2 years to drawdown then the income is subject to income tax. What this does mean is that beneficiaries who are in the process currently of deciding how to take death benefits, may wish to delay the payment of any lump sum until after 6 April 2015 to avoid or reduce the tax charge that may apply.

### Does inheritance tax (IHT) apply to pensions?

IHT normally does not apply to pensions, but there are specific occasions when it may apply and therefore you should speak to your lawyer or financial adviser for further detail.

### Keeping you up to date

We will continue to keep you up to date both online and via our customer magazines.

### Important Information

Alliance Trust Savings does not provide advice. Investments can go down as well as up. Investors may get back less than they originally invested. Tax rules are not guaranteed and may change in the future.

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