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New Pension Legislation Update - 9th December

Pension savers to get more freedom with their retirement money

Pension legislation that forms part of the draft 2011 Finance Bill will give pension savers a greater degree of control over how they use their retirement pots.
Under the draft laws, which were announced in the June Budget, the quasi-requirement to buy an annuity from an insurance company by the time someone reaches the age of 75 will be dropped from April 2011.

Pension Lump Sum
Pension savers will be afforded much more flexibility over how and when they take benefits under the new rules.

The current rules normally permit savers to take a maximum 25% of their pension pot as a lump sum but the proposed rules will allow savers to take much higher lump sums if their circumstances permit.

If savers can demonstrate that they have secured pension income (State Pension, Occupational Scheme Pension and Annuity income) of at least £20,000 per annum, they will be able to take the remainder of their pension pot as a taxable lump sum.

Income Drawdown
For those who are unable to meet the above requirements or perhaps want to remain invested to take advantage of the tax benefits afforded by a pension, the rules regarding income drawdown are also changing:

Under the current regime:

- The maximum income limit is 120% of a single life annuity rate (GAD) before age 75
- Drawdown reviews occur every 5 years before age 75
- Drawdown reviews occur every year after age 75
- Tax charge on death before age 75 is 35% if taken as a lump sum
- Tax charge on death after age 75 is up to 82% if taken as a lump sum

Under the proposed regime:

- The maximum income limit will be reduced to 100% of GAD
- Drawdown reviews will occur every 3 years before age 75
- Drawdown reviews will occur annually after age 75
- Tax charge on death will be 55% pre and post age 75

Death Benefits
Aside from the change to the drawdown death benefit rules detailed above, death benefits will broadly remain the same. If benefits have not been vested (or crystallised) before age 75 then the whole of your pension can be passed to your beneficiaries free of tax. If death occurs after age 75 then benefits will have been deemed to have been vested (regardless of whether any income has been taken) and the 55% tax charge will apply.

As is the case at the moment, your beneficiaries can choose to take the benefits as pension income instead which will be taxed at their marginal rate.
Many pension experts, however, are predicting that most savers will continue to buy annuities, which usually guarantee an income for life. A Treasury spokesman said: "The existing rules which create an effective obligation to purchase an annuity by age 75 will end from April next year. This will give individuals more choice over the use of their pension savings to provide a retirement income for themselves."

Reduced Limits
The Treasury announced in October that the annual limit will be cut from £255,000 to £50,000. Also to be reduced is the lifetime allowance on money that can be saved in a pension fund for which tax relief is allowed. This will come down from £1.8 million to £1.5 million.

The new annual allowance comes into effect as from April 2011 and the new lifetime allowance from April 2012.

To protect individuals who exceed the annual allowance due to a one-off 'spike' payment, the government is to allow them to offset this against unused allowance from previous years.