Financial Planning infobyte 2014

scruttonbland
accountants tax advisers insurance brokers financial advisers

August 2014 Professional Update

Neil G Hewitt
CFP, APFS, AIFP
Chartered Financial Planner

James Wright
BA(Hons), DipPFS
Independent Financial Adviser

Timetable announced for April 2015 Changes

The minutes of the HMRC Pensions Industry Stakeholder Forum held on 17 April 2014 set out the timetable for the introduction of the April 2015 pension benefit flexibility changes, announced in the 2014 Budget.

HM Treasury will be looking to introduce a Pensions Tax Bill in autumn this year which will enact the tax legislation, with a technical consultation on the draft legislation taking place in August.

HM Treasury is in the process of arranging technical working groups to discuss how best to achieve the Government's policy aims through its tax legislation. These groups will focus on six areas:

- the definition of defined benefit and defined contribution in HMT/DWP legislation
- tax planning and avoidance
- new products and innovation
- raising the minimum pension age
- the 55% tax charge on death, and
- the interaction between pension tax rules and pension scheme rules.

The introduction of these changes by April 2015 represents a very major challenge. It seems likely that, but for the looming general election in May 2015, these changes would have been implemented over a much longer time span.

If the April 2015 date is to be met, it is essential that providers and advisers have a thorough understanding of the new rules. While a technical consultation on the legislation is to be issued in August, providers and advisers will be awaiting the finalised provisions.

It seems likely that these will not be available until the early autumn, leaving providers around 3 months at the most to amend their systems. Even then, many providers may not be prepared to make any changes until the legislation is enacted.

New Pension Changes

Q: If my client's pension is paid as a lump sum, how will it be taxed?
A: The amount over and above the Tax Free Cash (or PCLS as it should be known) will be added to any other income in the year of payment and taxed accordingly. Large pension payouts could therefore push the client into a higher tax band.

Q: These new changes are currently subject to consultation. When are we likely to get more information from the Government on how the new rules will work?
A: The consultation closed on 11 June and the Government will now consider the feedback from the industry. There is no official deadline by which a response needs to be published but the minutes of a recent HMRC stakeholder forum confirmed that they are hopefully looking at publishing the Consultation Response soon.

Q: If the client needs income now but still wants to potentially take advantage of the new rules from April 2015, what can they do?
A: A Fixed Term Annuity or Capped Drawdown plan would allow some benefits to be paid out now and, according to the Consultation paper, would still allow the client to take advantage of the new rules from April 2015, if they wished.

Q: Why did the Government tweak the Triviality and Flexible Drawdown rules if a client can take all their benefits out as a lump sum from next April?
A: These changes are simply to allow some added flexibility in the run up to April 2015. As such, they are temporary measures.

Q: My client has an existing Capped Drawdown plan that was set up on 10 January 2014. When does the maximum GAD income level increase to 150%?
The new 150% GAD limit comes into force straight away for Capped Drawdown plans set up on or after 27 March 2014. For existing plans, it only starts from the anniversary date of the policy, which is 10th January 2015 in this client's case. There is nothing at all that can be done to change this.

Q: The Government announced that they are looking at banning transfer from final salary schemes. When is this likely to come into force?
A: Transfers from Public Sector final salary schemes will be banned and the Consultation is currently considering whether to impose a similar ban or some other restrictions on private sector final salary scheme transfers. No details have been published but we expect this ban to come into force from April 2015?

Pensions & Means Testing - Reminder?

It is important to understand how uncrystallised pension rights impact on a Member's ability to claim certain means tested benefits, especially in the light of the proposed new retirement benefit flexibility from next April. This Bulletin will focus on the current treatment of uncrystallised pension rights.

When considering means testing, advisers should be aware that the DWP uses the concept of the 'amount of notional income' to which a claimant is entitled. For occupational pensions, benefits are generally only taken into account from the scheme's normal retirement age, but for other pensions, notional income is considered from age 55.

The DWP guidance to Decision Makers (DMs) states 'DMs must consider evidence from pension fund holders when deciding the amount of notional income'. Where a pension allows income drawdown, the notional income is deemed to be the maximum income permitted under legislation, i.e. currently 150% of GAD.

However, with the advent of retirement benefit flexibility from next April, the concept of maximum GAD will, we presume, fall away, as capped drawdown will no longer apply. However, the Government cannot afford to ignore the capital (uncrystallised benefits) that an individual has accumulated in their pensions, if it means they would otherwise be able to claim state benefits. The way in which the new retirement benefit flexibility will impact upon the way in which notional income is calculated, needs to be considered.

In a question and answer session (link at the end of this piece) with the Work and Pensions Select Committee on 30 April 2014, the Secretary of State for Pensions, Steve Webb, clarified the Government's position regarding the impact of the new pension tax rules on means testing, 'we need to think through—for all of the different types of capital and income people will have, and for all of the different things we means test, which is Pension Credit, Housing Benefit, social care and all the rest of it—a consistent approach to these things. Coming back to my reply to Debbie, the intention is not to fundamentally change the way we treat these things.'

So, it is possible that the notional income could be based upon an annuity rate, but perhaps it is more likely that the DWP will apply their existing basis for calculating notional income from capital sums.

Currently, the DWP has a formula for calculating a claimant's notional income from capital.

Once an individual has capital in excess of the capital disregard (typically £10,000, but can be a lower disregard of £6,000 for certain benefits) it is deemed to generate an income of £1 per week for each £500 (or part thereof) of capital. So an individual who has capital of £10,000 in excess of the appropriate capital disregard, would be treated as having a notional income of £20 each week.

As yet, it is not known how the DWP will deal with this. However, it is unlikely to be addressed in the proposed Pension Tax Bill due in the autumn and will more likely be addressed in specific DWP Regulations, issued later in the year.

So, what is the alternative for clients who are on, or potentially will be on, means tested benefits and have relatively small uncrystallised pension rights?

If a client is being adversely penalised by having uncrystallised pension rights, one option is to crystallise them. Once crystallised, what should be done:

- an obvious option would be to clear any outstanding debts, perhaps with the exception of a mortgage, which in itself could result in higher benefit payment

- alternatively, securing a lifetime annuity with some of the pension rights may be an attractive option. This is a low maintenance solution and will generate an income which will impact upon benefits, but the income is secure and, more importantly, the income is only assessed at face value, and as such has a much less detrimental impact upon the benefits received.

The main means tested benefits that are likely to be considered include:

- Pension Credit
- Income-based Jobseeker's Allowance
- Income-related Employment and Support Allowance
- Working Tax Credit
- Child Tax Credit
- Housing Benefit

The new Universal Credit is replacing each of these benefits, except for Pensions Credit and is still in the process of being rolled out nationally.

Commutation of Small Pension Funds - Enhanced Tax Free Cash & Segmentation

In 2009, regulations were introduced which allowed occupational pension schemes to commute small pots valued at less than £2,000, subject to certain conditions known as the 'stranded pot' rule.

These rules were then extended in 2012 to allow individuals to commute benefits valued at under £2,000, if they were held within a personal pension plan, known as the ‘small pot’ rule.

More recently, from 27 March 2014, the 'small pots' / 'stranded pots' limits were increased up to £10,000.

There are a few features of these rules which it is worth focusing on so that you can ascertain whether your client qualifies for this type of triviality payment. The common qualifying conditions are well known and are listed here:

1. You only need to consider the value of the benefits in that particular pension arrangement and not all benefits the client has in total.

2. The client has to be over age 60 before this payment can be made.

3. The client can have 3 of these payments in total.

4. The rules apply at ‘arrangement’ level rather than at policy or scheme level. If the pension plan is set up with a number of arrangements or segments (e.g. one for former protected rights and one for non protected rights) it would allow the rules to apply to each segment in isolation. So, a client with a policy valued at £29,700, firstly needs to check if the policy is already segmented and if not, could ask the provider to re-shape the plan into 3 segments of £9,900 each which would allow 3 'small pots' payments to be made.

5. These small pot payments can be made in addition to any standard trivial commutation lump sum payments. So, imagine we have a client that has 4 policies, 3 of which are valued at £9,000 and one valued at £25,000. The client has the 3 small pots paid out. He then only has one policy worth £25,000 and qualifies under the normal Triviality Rules to have this paid out as well.

6. The final quirk only relates to occupational schemes such as EPPs and SSAS. Firstly, you need to check that there has been no transfer out of the scheme or any related scheme within the last 3 years. Then we need to check whether the policy allows a higher than 25% entitlement to Tax Free Cash (TFC). If so, then the rules allow the enhanced TFC to be paid out and, if the remaining money in the scheme is valued at below £10,000, then it can be paid out under the stranded pots rule

For more information please contact:

Ipswich:	**01473 267000**
	Fitzroy House, Crown Street, Ipswich, Suffolk, IP1 3LG
Neil Hewitt	**Neil.hewitt@scruttonbland.co.uk**
James Wright	**James.wright@scruttonbland.co.uk**
Colchester:	**01206 838400**
	820 The Crescent, Colchester Business Park, Colchester, Essex, CO4 9YQ
Gary Riches	**Gary.riches@scruttonbland.co.uk**
Grant Buchanan	**Grant.buchanan@scruttonbland.co.uk**