



Pensions – Not so Simple Simplification

What Pension Tax Simplification could mean to you and your pension scheme

Following publication of the Finance Bill we now know that pension tax simplification will proceed and that 'A' day will be 6th April 2006. Other changes are contained in the Pensions Bill currently before Parliament.

To help consider some of the changes and implications for schemes, which will affect employers, trustees and members, a quick recap of the main headlines would perhaps be appropriate:

To Plan or not to Plan

Allowances

- Any individual may have a pension value of £1.5m (the Standard Lifetime Allowance, SLA) from A - Day.
- The accrued pension entitlement of final salary schemes before vesting have a 20:1 factor applied to them to determine their current monetary value for comparison against the SLA.
- Benefits in payment at A-Day will be valued on a 25:1 basis, using the annuity being received.
- On death or retirement excess funds above the SLA are subject to a 25% Recovery Charge. If the excess fund is taken as a lump sum the Recovery Charge is 55%.
- Annual contribution allowance of £215,000 from April 2006 rising to £255,000 in April 2010.
- Any UK resident individual can pay £3,600 or, if higher, 100% of earnings up to the annual allowance each year and receive the tax relief. Employer contributions are included in the annual allowance.
- Final salary scheme increases in benefit each year use a 10:1 factor for monitoring the input limit.
- Excess contributions over the annual allowance may result in a tax charge on the member.

Retirement and death benefits

- From 2010 benefits cannot be taken before age 55, and must be vested before age 75.
- Subject to certain conditions existing, early vesting dates will continue for those already contractually entitled.

- 25% of the individual's fund (subject to the SLA) can be taken as a tax-free cash sum.
- Income can be secured by annuity, via drawdown or from age 75 by alternatively secured pension.
- Prior to vesting, the fund value (subject to the SLA) may be paid as a lump sum on death with no tax charge. Any excess above the SLA may be paid as a lump sum subject to 55% tax.
- On death post vesting, but prior to age 75, a capital payment less a 35% tax charge can be paid.
- On death after age 75, no return of capital is normally allowed. However, in certain circumstances there may be opportunities for capital preservation with the new alternatively secured pension.

Investments

- There will be one regime for all pension schemes, with provisions to retain existing investments post A Day where required.
- Property investment will be extended to include residential holdings.
- There will be a 5% of fund restriction on investment in sponsoring employer shares.
- No loans to members will be permitted.
- Employer loans will be restricted to 50% of the fund value, subject to security and a maximum term of 5 years, with a provision for one 3-year extension.
- Borrowing will be restricted to 50% of the value of scheme assets.





Birmingham:	0121 237 1300	Leicester:	0116 247 3600
Bristol:	01275 371 871	London:	0207 891 2661
Edinburgh:	0131 226 8300	Manchester:	0161 233 7090
Leeds:	0113 232 1100	Plymouth:	01752 607 660

Implications for schemes and employers

The proposals for pension simplification send a bulldozer through much of the existing rules. Post A-day many of the distinctions between occupational and personal pension schemes will disappear.

All employers who currently run occupational schemes for their staff must consider these changes. Changes in death benefit rules mean that a review of group life arrangements may be appropriate, or even necessary.

Implications for trustees

Pension scheme trustees need to be aware of the need to check and amend scheme rules to fit in with the new legislation in the Finance Bill.

At the same time important changes are included in the Pensions Bill and these also need to be incorporated:

- It will no longer be possible for schemes to opt out of member trustee election.
- Trustees must demonstrate a higher level of knowledge than at present.
- The schemes rules and documents will need to show the new limits and allowances.
- All benefits bought for members of occupational pension schemes with less than 50 members must be secured by annuity purchase. The member must also be offered an open market option.
- Schemes must provide more comprehensive and regular information to members. An allowance of £150 per member for professional advice will be introduced without a benefit in kind charge applying and this will also qualify for corporation tax relief.

Scheme trustees will be responsible for administering and collecting the recovery charge where the lifetime limit is exceeded.

If there are members earning in excess of the earnings cap (£102000) account needs to be taken of the fact that this will be abolished in 2006.

Definitions of salary and pension benefits may need amending, as may contracts of employment. Alternatively the employer will need to fund for the consequent additional benefits which will accrue for such members.

Implications for scheme members

Transitional Arrangements

There will be an opportunity to protect against the Recovery Charge through one of two types of protection, Primary or Enhanced.

Primary protection

- Primary Protection may be selected for those with pension values more than £1.5m at A-Day, who wish to continue active scheme membership.

Enhanced Protection

- Enhanced Protection may be selected for funds of all sizes and may be suitable for those wishing to protect future fund growth from the Recovery Charge. Post A-Day contributions are not permitted. Both Primary and Enhanced Protection rights must be registered with the Inland Revenue.

Tax-free Cash Sum Protection

It is also possible for an individual to protect their tax-free cash sum entitlement where it is more than 25% of their fund or above £375,000. However, only those who have registered for Primary or Enhanced protection and have a cash sum above £375,000 will be able to transfer their funds after A day and still retain their right to the higher entitlement. Everyone else will lose their higher entitlement if a transfer is made after A-Day.

Identifying and then ensuring these pension assets are held in the most appropriate arrangement at A-Day will therefore be of critical importance.

With this array of change there is a compelling need to be proactive to the circumstances of scheme members. Although transitional protection may be registered up to three years after A-Day, for many (perhaps all) members the planning and analysis will have to take place **before 06/04/06**, or run the risk of precluding certain planning strategies. It will often be necessary to undertake a comprehensive audit of all other pension benefits. All of these tasks will take time to achieve.

Summary

As ever, each scheme's circumstances will be different. The key to success as we approach A-Day is to have in place a robust strategy which revisits:

- Identifies the members most in need of advice
- Collates and analyses all relevant pension scheme assets and
- Revisit the best type of scheme to suit your company's needs.

LEBC Group Ltd. with its expertise in pension scheme issues is able to help employers and trustees come to terms with the changes and to give individual advice to scheme members. If you would like to discuss the implications for your scheme please contact your usual LEBC adviser, complete the enclosed card or e-mail us at pensions@lebc-group.com.

