

PENSIONS A-DAY (6TH APRIL 2006)

JOHN M TAYLOR & CO

CHARTERED ACCOUNTANTS & BUSINESS ADVISORS
9 GLASGOW ROAD, PAISLEY, PA1 3QS
TEL: 0141 848 7474; FAX: 0141 848 7419;
EMAIL: MAIL@JOHNMTAYLOR.CO.UK



Pension Reforms

Why are they changing?

Current pension rules are complicated and cover a range of different types of pension scheme. On 6th April 2006 these pension rules will effectively be abolished and replaced with a new pensions regime which will cover all schemes.

Due to the fact that people are living longer the amount the government pays out each year in the form of the basic State Pension is increasing. However, the number of workers paying national insurance into the system is not increasing which poses a big problem for the government.

In addition to this, many UK workers are not making adequate provisions for their retirement in the form of private pensions. The government will therefore implement the new pensions regime from 6th April 2006 to simplify private pensions to make them easier to understand and thereby encourage us to save for our retirement.

In this guide we intend to give a brief overview of the main changes which will result from the governments simplification of the pension regulations.

Summary of main changes

Annual Allowance

No limit on contributions paid by an employer to a pension scheme. However, if total contributions exceed £215,000 in any tax year the individual will be assessed for income tax on the excess contribution. This annual allowance will increase to £255,000 by 2010.

Member contributions

Within the £215,000 allowance, member contributions will be eligible for tax relief if the personal contributions in any tax year does not exceed the higher of £3,600 or 100% of net relevant earnings for that year.

Net Relevant Earnings are calculated as the total of your employment earnings (i.e. salary plus benefits in kind less employment expenses) and/or self employment earnings (less capital allowances and losses carried forward). Should you received income from furnished holiday letting this income also counts for net relevant earnings purposes.

Lifetime Allowance

Individuals will have a lifetime allowance on the value of their pension scheme at retirement. At 6th April 2006 this allowance is set at £1.5 million but this figure will rise each year until it reaches £1.8 million in 2010.



Minimum Pension Age

By 2010 the minimum age at which a company pension or private pension can be taken will be 55. Should you be however be unable to work due to ill health it is possible that his rule will be relaxed.

No carry back

The current facility to carry back pension contributions to a previous year to utilise unused pension allowances will be abolished. This means that should you wish to make pension contributions during a particular tax year you should ensure that the contributions are paid prior to 5th April so that tax relief is available during the desired tax year.

Recovery Charge

At retirement the value of the pension scheme will be valued against the lifetime allowance at that point. Any excess can either be taken as a pension and subject to a tax charge of 25% or taken as a lump sum and subject to a tax charge of 55%.

New Pensions Rules

1. By April 2010, the minimum age at which you'll be able to take your company or personal pension will have increased from 50 to 55 unless you are unable to work due to ill health.
2. An Annuity, alternatively secured pension or scheme pension may continue to be paid during a 10 year guaranteed period.
3. The facility to carry back pension premiums to a previous year to utilise unused tax reliefs has been abolished.
4. Pension schemes can pay a tax-free lump sum of up to 25% of the fund value (up to a maximum of £375,000).
5. If you are a member of a company pension scheme you will no longer need to leave your job before you can draw your pension subject to the rules of your particular pension scheme.
6. Between 2010 and 2020 the age at which women can claim their State Pension will gradually increase from 60 to 65.

(As every pension provider has different rules and requirements it is necessary to check with your pension scheme to determine the exact details of the scheme.)

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Maximum Pension Age

No pension contributions can be paid after the age of 75 as pension benefits must come into payment by age 75.

Employer Contributions

Employer Contributions are unlimited and will be granted corporation tax relief. The Finance Act also introduces provisions for tax relief on employer contributions to be spread where contributions exceed both 210% of the contributions paid in the previous chargeable period and £500,000. This applies to all types of pension scheme.

Lifetime Allowance: Pre A-Day Rights

There are two mechanisms for protecting pension rights accumulated prior to A-Day. These are primary and enhanced protection and will benefit those who have accumulated significant benefits before A-Day.

Primary Protection

This is available to anyone who is still contributing to a registered scheme or who are still in pensionable service when the value of their pre A-Day pension rights exceeds the lifetime allowance.

The pension rights protected from the lifetime allowance charge are calculated as a percentage of the lifetime allowance and this percentage is protected against any future lifetime allowance charge.

Enhanced Protection

Enhanced protection is available to anyone who leaves pensionable service and stops contributing to a registered scheme. This is available regardless of whether or not their pre A-Day pension rights exceed the lifetime allowance at registration.

Essentially if an individual elects to claim enhanced protection they are unable to make further contributions to a defined contributions scheme or to accrue further benefits. However, growth in line with salary or investment growth is permissible.

The main advantage of enhanced protection over primary protection is that it enables an individual to take advantage of growth in their investment or salary increases without becoming liable to the lifetime allowance charge (subject to certain restrictions).

Increased Lifetime Allowance

There are also a variety of other scenarios where an increased lifetime allowance may be permissible.



In the following circumstances an extra percentage may be given on top of the standard lifetime allowance:-

- Pension Credits received before A-Day
- Rights built up during a period in which an individual was not resident in the UK.
- Pension Credits arising from a pension in payment which was acquired on or after A-Day.

Overall the new Pension Regulations which come into effect on 6th April 2006 will bring significant change to the way we save for our retirement. In particular those who are high earners and who have accumulated significant value in their pension fund are more likely to feel the effects of the new rules.

As all pension schemes are different you should contact your pension provider for more information on how you are likely to be effected by the new rules.

Important Note

This factsheet is provided for general information only and should not be relied upon to take action nor should it be seen as attempting to provide you with any advice. The issues covered are particularly relevant to high earners who have accumulated a significant pension fund with a value close to the lifetime allowance. The information contained in this factsheet represents our understanding of the new pensions regime which will come into effect on 6th April 2006. Where action is required it is important that you seek advice specific to your individual circumstances and requirements from a professional financial adviser.