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INVESTMENT BULLETIN

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THE EVER CHANGING WORLD OF PENSIONS

Like Marmite, people tend to love or hate pensions and for every individual seeking to maximise their funding, there is another who (perhaps mistakenly) feels that pensions are not for them. The aim of this letter is to summarise the key changes and our views on this . For some of you this may be irrelevant BUT I expect there will be many column inches and news articles on this in the coming months and if nothing else, it'll put you in the know!

CHANGES TO THE STATE PENSIONS

In April 2016 the state pension will finally move to a flat rate for all those subsequently retiring. There will be winners and losers but in the long run it will help people plan for their retirement whilst also removing the risk of people being disincentivised to save for themselves.

We are seeing the state pension age gradually rise and the 2014 Budget compounded this with anyone born after 1978 now having a state pension age of 68.

Recently we have also seen flexibility introduced whereby individuals can defer their state pension and subsequently benefit from a lump sum or an increase in their state pension once drawn— though contrary to the scams you may have well seen, you cannot 'unlock' your state pension!

Despite cynicism from some that the state pension 'won't be there when i retire', our view is that it provides a solid foundation to an individual's retirement income and whilst we cannot legislate future legislation, we feel that the importance of this as part of an individuals broader financial planning should not be overlooked.

AUTOMATIC ENROLMENT

Alongside the delays to the State Pension age, the Government at the time also legislated that all Companies will have to offer and pay into a pension for their staff through something known as 'Automatic Enrolment'.

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This has been a long time coming but in 2013 the legislation began to apply and the first (very large!) companies faced the challenge of ensuring they met the costs of the pension contributions whilst also covering the 'time cost' of the administration and compliance.

This will essentially apply to all businesses and as time moves on it will therefore impact on all companies, irrespective of size—noting that even the minority which are exempt need to be aware of their reporting responsibilities.

Yes, it can be argued as being a 'taxon employers' given that it is essentially shifting pension provision away from the Government onto the private sector but its important to focus on what is important and, in our view, grab the bull by the horns and ensure the legislation is satisfied as efficiently as possible.

PENSION FREEDOMS

As if the above wasn't enough change, Chancellor Osbourne announced what can only be explained as one of the biggest Budget shocks in recent memory – at least in financial planning circles – when he announced proposals to give people the freedom to access their pensions as they need.

Whilst the criteria remains that pensions can only (legitimately!) be accessed from 55, the proposals removed the restrictions on the amount of income that can be drawn and instead leaves the individual free to choose.

Whilst this change has not yet come into force, amendments to legislation took place immediately and these are paving the way to this 'brave new world'.
The new rules will therefore enable those over 55 to access their pensions as they see fit and as we outline below, we see some interesting opportunities.

In addition, the tax liabilities on lump sum death benefits are also improving; currently a pension fund not yet drawn can, in the event of death, generally be paid as a tax free lump sum. Once benefits begin to be drawn, however, tax of 55% would be applied to lump sum death benefits.

Under the new rules, whether a pension is drawn or not, lump sum death benefits will generally be free of tax for those aged up to 75; for those who are older, the tax charge will be based on the recipient's rate of tax and therefore could be as low as 0%.

Furthermore, in the past beneficiaries in many cases needed to be dependents – this requirement has been removed and therefore whilst much is made of the freedom to access capital, our view is that those who have saved hard over the years to fund for a happy retirement will perhaps find greatest satisfaction from the thought that more of their monies can be handed down the generations when the inevitable unfortunately happens.

PRACTICALITIES

Whilst much was made of the Lamborghini motorcar being the method in which those sensible enough to build up assets for their retirement will suddenly want to exhaust their hard earned savings - in reality we genuinely see these changes as opening up some interesting financial planning opportunities.

Removing the restriction to use the majority of the fund as an income does present the opportunity to spend the capital more aggressively – though this should not be a problem for those with sufficient lifetime income secured elsewhere. Doing so also opens up the scope of being clever with tax.

For example, those who retire early may well find that, in the years between leaving (self) employment and reaching their state pension age, their personal allowances go unused. Historically, private pensions could only partly help but the new rules will mean that for those with no other taxable income, withdrawals of up to £14,133 can be drawn tax free from their pensions (tax year 2015/16) by using their personal allowance. For a couple with no other taxable income, that equates to £28,266!

Clearly this is using retirement capital to fund an immediate lifestyle but for those who have additional and sufficient pensions provision into their old age, this flexibility opens up greater scope for a tax efficient early retirement.

Furthermore, given that pension assets are usually outside of an individual's estate, a pension will offer an immediate way of sheltering assets from Inheritance Tax and if these funds remain surplus to requirements, these assets can now be passed initially between spouses and then down to their children and then their children etc.

At a stroke, the rule changes removed a significant reason why some avoid pensions – the fact that, despite all of their tax efficiencies, you lose control of most of the capital; whilst that remains the case for those under 55 years of age, this will no longer be the case once the individual reaches the age at which private pension assets can be drawn (currently 55).

Historically, pensions have also been used as a tax effective means to remove funds from a business into the hands of the owner(s) – all of these changes further compound these benefits and add Inheritance Tax to the Income Tax and Capital Gains Tax reliefs pensions benefit from.

The genuine practicalities of the new rules are yet to be seen but for us, April 2015 cannot arrive soon enough. As such, we feel that it is very important that the very nature of pensions are looked at again and we hope that the points outlined above help to explain the significant change to the 'retirement landscape' which is about to unfold.

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