

retirement planning :

for financial advisers only

# increased flexibility

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## Adrian Walker outlines upcoming changes to Protected Rights and the associated retirement planning opportunities.

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Much interest has been focused on the introduction from April 2012 of personal accounts and the auto-enrolment of employees into these arrangements or alternatively qualifying registered pension schemes. The debate surrounding these changes, however, may have allowed the significant alterations to Protected Rights from that tax year, which will affect many individuals' short- and long-term retirement planning, to escape attention.

### what will change?

From the 2012/13 tax year onwards, contracting out of S2P on a money purchase basis will cease, although registered schemes will still receive rebates from contracting out for the 2011/12 tax year for some time after that date. The differential between Protected Rights and non-Protected Rights will disappear from 2012/13, with all money purchase rights built up within a registered pension scheme becoming non-Protected Rights.

For many individuals Protected Rights forms a significant part of their money purchase funds, and this structural change will cause significant issues for ongoing financial planning. The key areas impacted are outlined below.

### statutory money purchase illustrations (SMPI)

From October 2009 SMPIs will begin to take the 2012/13 changes into account. Many clients will therefore see a reduction in projected pension rights, which previously assumed rebates would continue until state pension age.

From the beginning of the 2012/13 tax year clients will accrue entitlements within S2P,

although capped to earnings below the Upper Accrual Point of £40,040.

Skandia's SMPIs will assume that no further rebates will be received in the period leading up to April 2012, as many clients deal directly with the Department for Work and Pensions when considering contracting out. If further rebates are received in this period, clients will see a benefit increase in future illustrations.

### pension commencement lump sum (PCLS)

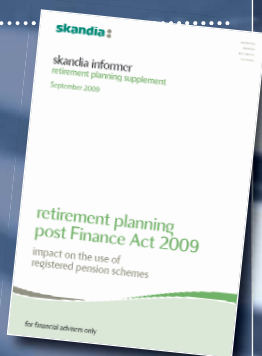
The available Protected Rights PCLS is limited to 25% of the fund value built up from those rights. When those rights become non-Protected Rights from 2012/13, this restriction will no longer apply.

For clients with pre A-Day protected cash entitlements including an element of Protected Rights (eg from benefits originally held in pre A-Day contracted-out money purchase schemes), more of the Protected Rights may be available to be taken as a PCLS. For some clients this could be a significant amount. The effect on the actual monetary PCLS that becomes available could be substantial. Where clients would benefit by delaying benefit crystallisation from such schemes until the changes come into effect, this could create significant opportunities for retirement planning advice.

The PCLS issue is also relevant for clients holding Protected Rights funds in S32 contracts where protected cash is currently available. Legislation does not currently allow income withdrawal from Protected Rights held within such contracts, but this restriction will disappear when the changes come into effect.

# retirement planning post Finance Act 2009 – Impact on the use of registered pension schemes

With this issue of **informer** you have received our special **retirement planning post Finance Act 2009** supplement, outlining new financial planning issues that need to be taken into account with regard to current and continued use of registered pension schemes as part of a retirement planning strategy. If you did not receive a copy but would like one, please e-mail [informer@skandia.co.uk](mailto:informer@skandia.co.uk)



## annuity purchase

On the death of a married member, any annuity currently purchased from Protected Rights must provide a contingent annuity for the member's spouse\*, and the annuity rates used are on a unisex/unistatus basis.

The changes coming into effect on April 2012 will eliminate these issues, allowing clients greater freedom of annuity choice. The removal of unisex/unistatus requirements should also mean improved annuity rates become available for males. Clients will also be able to phase their Protected Rights into retirement income.

## income withdrawal

Not all providers currently offer income withdrawal from Protected Rights, although it may be offered on non-Protected Rights. The April 2012 changes should open up a wider choice of income provision.

The income factors provided by HM Revenue & Customs for Protected and non-Protected Rights income withdrawals will remain unchanged. However, while income taken from crystallised Protected and non-Protected Rights currently has to be drawn proportionately from both elements, it may be increasingly important in the run up to the changes that where the client concerned is married, Protected Rights are held in a registered scheme offering income withdrawal on those rights.

If a married client were to die prior to April 2012, any Protected Rights fund must be used to provide income to the spouse. If the scheme does not offer income withdrawal for Protected Rights then the only option is to secure a Lifetime Annuity, which (due to age) may not be the best option for the spouse. Access to a dependant's income withdrawal facility will avoid this problem and allow the spouse to defer, if necessary, taking any income.

Consolidation of existing Protected Rights funds into schemes offering such facilities could still be paramount, given that death is the one issue which can't be planned for.

## death benefits

As already mentioned, where a client is married any Protected Rights must currently be used to generate income on the client's death, a requirement which will disappear from April 2012. The total value of benefits within the client's available Lifetime Allowance can instead be paid as a lump sum.

Where this is from uncrystallised funds, the payment will be tax-free. From crystallised funds, income withdrawal will trigger a withholding tax charge (currently 35%).

The April 2012 changes will also affect the basis of any lump sum disposal by the scheme trustees. Where Protected Rights are paid as a lump sum on death of a person who has no surviving spouse or dependant, there is currently no discretion available to the scheme trustees as to who receives the benefit. It will instead go to the parties nominated by the member, and if there has been no nomination (or the nominated beneficiary no longer exists) the benefit will be paid to the deceased member's estate, potentially subjecting the payment to inheritance tax.

Where a member dies after the changes, this restriction will no longer apply and full discretionary disposal of any lump sum from these rights becomes available.

## summary

The 2012/13 changes will not only affect clients with Protected Rights entitlements already in money purchase schemes. Clients who may be considering benefit transfers from contracted-out defined benefit schemes will also need to be aware of the future implications. The eventual structure and flexibility of both retirement and death benefits for the Protected Rights included in the cash equivalent need to be understood when such an important decision is taken.

While the 2012/13 tax year is still some way off, there is nonetheless a need for advice in the shorter term to ensure clients are not only aware of the implications but can make the necessary changes in order to benefit fully. ●●

For further information and support about the changes to Protected Rights please contact your Skandia consultant or regional office.

\*Or civil partner as defined by the Civil Partnership Act 2004.

This article is based on Skandia's interpretation of the law and HM Revenue & Customs practice as at August 2009. We believe this interpretation to be correct but cannot guarantee it.

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