

prepare for the big freeze

January 2009

Adrian Walker takes a closer look at the impact of the Pre-Budget Report on retirement planning.



In last month's *informer* Colin Jelley outlined some of the major advice issues arising from the Chancellor's Pre-Budget Report (PBR), several of which may impact on clients' future retirement planning. In this article I will address those proposals where the impact is more immediate, rather than those announced for introduction beyond the 2009/10 tax year.

lifetime and annual allowance

The PBR announced that the Lifetime Allowance and Annual Allowance applicable for the 2010/11 tax year will remain frozen until the end of the 2015/16 tax year. This announcement will impact upon future retirement planning for some clients using registered pension schemes.

The A-Day legislation only guaranteed the Lifetime and Annual Allowances would not reduce below that of the previous tax year. This allows the Government to position the proposals as simply an early announcement of the next five-year planning period. It is interesting to note, however, that the PBR Technical Annex estimates that this freezing of both allowances will save £325 million before

the 2011/12 tax year. In that year alone the estimated savings to the Treasury increase to £400 million.

Freezing the Annual Allowance at £255,000 a year will impact few clients, but may be an issue for higher earners where:

- they wish to take advantage of the ability to contribute up to 100% of their relevant earnings, or
- will receive significant contributions direct from their employer.

By using the ability to change pensions input periods, these clients will still have the opportunity to fund up to £510,000 of contributions without needing to take immediate benefits or being subject to an Annual Allowance charge.

Of course, the ability to increase their provision using the current Annual Allowance and that of the 2009/10 and 2010/11 tax years will make a significant dent in their available Lifetime Allowance. For such clients, there is scope to fund £735,000 of contributions over the remaining three tax years of the current cycle. Funding at this level, will, when added to any existing pension fund value, undoubtedly reduce the need for further funding above a future Annual Allowance.

The Annual Allowance may, however, be irrelevant where clients are funding close to retirement. Provided the client fully crystallises the benefits under the arrangement receiving the contribution by the end of the tax year in which the pension input period ends, the contributions will form no part of a client's Annual Allowance.

It is important to consider whether this 'freezing' of the Lifetime Allowance is temporary or the first stage of something more permanent. Clients who are intending to crystallise benefits beyond the 2015/16 tax year will, along with their financial advisers, need to take a view on funding over the next eight years or so. It might well be sensible to consider funding no more than the known Lifetime Allowance of £1.8 million, until the picture beyond 2015/16 is clearer.

A-Day fund protection

In December's *informer* I highlighted the closedown date for clients wishing to register their pre A-Day pension rights for Enhanced and/or Primary Protection. The freezing of the Lifetime Allowance will affect clients even if they register for Primary Protection, as their personal Lifetime Allowance will not increase for the five-year period beyond 2010/11 tax year.



A review of when to consider crystallising benefits is now essential. Any excess capital crystallised beyond a personal Lifetime Allowance will subject the excess to a Lifetime Allowance charge of 55% if taken as capital, or 25% if taken in the form of income (with income tax then being charged). With higher rate income tax scheduled to rise to 45% in the 2011/12 tax year, the Lifetime Allowance charge may also rise, making the tax treatment of the excess rather less attractive.

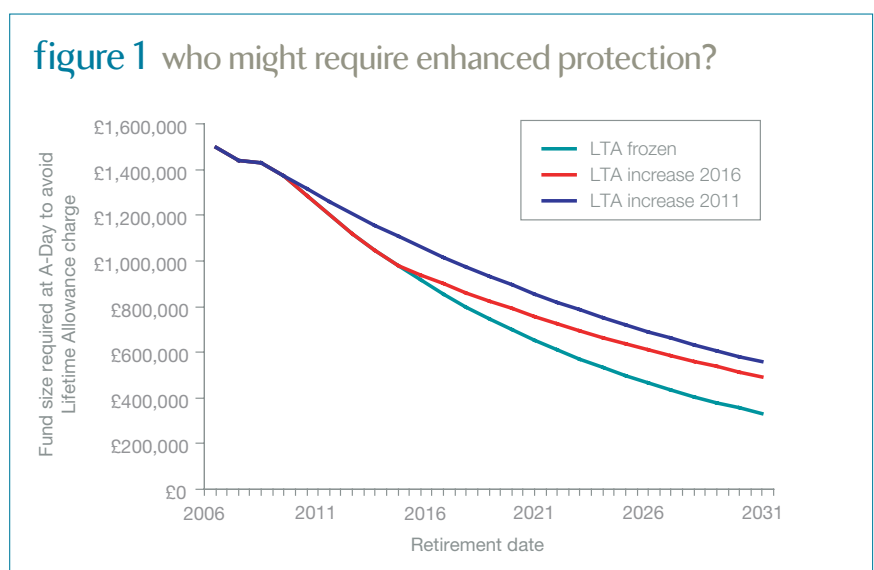
Clients with a Defined Benefit based scheme may want to consider whether it is worthwhile to opt-out of future accrual that could result in a Lifetime Allowance charge – or take benefits early to reduce the impact of a possible charge.

For clients who have had no benefit accrual since A-Day in registered pension schemes, the freezing of the Lifetime Allowance means there is a need to review whether to register their pre A-Day pension rights for Enhanced Protection. They will need to think about the likely future investment returns on their existing pension rights, when they may be looking to crystallise their benefits and whether the Lifetime Allowance will again increase beyond 2015/16 tax year.

Figure 1 highlights how the A-Day fund value might be at risk of breaching a future Lifetime Allowance now we are aware of its value from 2011/12. The graph assumes the A-Day fund value will grow at 7% a year after all charges. The three lines assume firstly that the Lifetime Allowance would increase by 2.5% a year after 2010/11 (ie reflecting an assumed position before the PBR), secondly that the Lifetime Allowance will increase from 2016/17 by 2.5% a year, and thirdly that the current Lifetime Allowance will not increase at all.

The value of pre A-Day rights that may be at risk if a client does not register for Enhanced Protection when eligible to do so varies significantly between these assumptions.

In summary, it is clear that clients affected by the changes applying to pension schemes will need expert financial advice to help them adjust their retirement planning strategies to take into account these most recent changes. ●



Lifetime Allowance assumed to increase by 2.5% a year. Fund growth 7% a year net of product charges

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