

IFA Fact-Files
"Pension A day issues"
6th April 2006

PO Box 87, Crockenhill
Swanley, Kent BR8 9AP

Tel: 01322 669059

Fax: 01322 666825

Email: martin@maaltld.co.uk

Web: www.maaltld.co.uk

Series 3

EXISTING PENSIONS

(Other A day fact-files: Contributions & Pension Benefits)

As from A day, there will be a different set of rules governing the way you can draw money from a pension scheme. Importantly of course, all pensions will be governed by the same rules as of 6th April 2006. There are however certain **transitional** arrangements that you may need to consider to **protect** your pension and there are some other issues that we feel it is right to bring to your attention. We split this fact-file down into some of the pension groups that are currently available pre A day.

Personal Pension funds (including SIPPs)

The rules are changing so that all other pensions will become very similar to Personal Pensions. These are the simplest form of pensions enabling the holder to receive 25% tax free with the remaining fund used to purchase an income for the rest of your life. There is nothing really to change or be aware regarding your pension as a result of A day except that:

- Carry Back will be abolished.
- Contributions can now be up to £215,000 in the first year.

Section 226 Retirement Annuities

These were the fore-runner to Personal Pensions and had to be taken out before 1987. Tax free cash is likely to be lower than 25% of the fund with an old S226. It is currently possible to pay a larger % of salary/earnings into a S226 depending on age.

After A day, it is likely that most S226 holders will be in a better position as far as tax free cash is concerned and under the new rules much higher contributions can be paid. There are relatively few of these policies still in existence.

Executive Pensions (including Small Self Administered Schemes – SSAS)

Taken out by many Company Directors these plans are subject to the most changes and planning issues at, before and after A day. The eventual benefits (pension and tax free cash) under these plans are linked not only to how much is in the pension fund, but also to the individuals' Final Salary (excluding Dividends), their length of service with the company and the rules under which their scheme was established. The *maximum* pension is always however **2/3rd** of Final Salary and the *maximum* tax free cash is **1½** times Final Salary:

Final Salary – for a Company Director this is always the best 3 or more consecutive years pensionable earnings not ending 10 years before normal retirement age.

Scheme rules – are related to the year the scheme was established and the date the member joined the scheme. It can be either:

- Pre 1987
- 1987 to 1989
- Post 1989

Service – the maximum pension and cash benefits available depend on the individual's length of service with the company, but also depends on the scheme rules applicable.

Example Executive Pension benefits:

If a member of a Pre '87 scheme were retiring at their normal retirement age on an averaged Final Salary of £150,000 having completed at least 20 year's service with the company, the benefits available would be as follows:

Tax free cash	£225,000
Pension	£99,000 per annum

Executive & SSAS pension - continued

On the previous page are the *maximum* benefits. In order to provide these benefits there must be sufficient in the pension fund to pay out this level of cash and income. In this case the fund probably needs to be worth in excess of £1,800,000 (scenario 1). It is quite likely in this case that there isn't this level of funds available in the pension. Let's assume there's only £500,000 in the fund (scenario 2).

As far as A day is concerned, you need to be informed about the level of tax free cash you are entitled to as a % of your total fund.

Less common scenario

With scenario 1, the tax free cash is £225k from a fund of £1.8m giving tax free cash of 12%. In this scenario, the individual probably needs to apply for **Primary Protection** of the fund as it is over the Lifetime Allowance (see A day fact file series 2 – Pension benefits). This will enable them to continue paying into the pension whilst ensuring that excess benefits will be not be taxed too punitively. Schemes must be registered by 5th April 2009.

More common scenario

With scenario 2, the tax free cash is £225k from a fund of £500k giving tax free cash of 45%. At A day all tax free cash is reduced to 25% unless entitlement to higher tax free cash can be proved or has been previously certified. Whilst there is no *necessity* to take action at this stage, it is imperative that individuals in this scenario are receiving advice now as:

- They need to be able to prove earnings, length of service etc.
- If they *transfer their funds after A day*, their higher tax free cash entitlement will be lost. For those seeking to make changes NOW (because of poor investment performance or heavy charges primarily) they must do this pre A day to preserve their benefits – probably using a S32 contract.

As well as Primary Protection there is **Enhanced Protection** which is for individuals whose pension fund is not currently over the Lifetime Limit but who expect their fund to be in excess of the Lifetime Limit by the time they wish to draw their pension. Those who apply for Enhanced Protection will not be able to pay anything more into their funds after A day.

Other Pension Protection issues

- Protection of pension funds can also apply to large Personal Pension funds.
- Individuals have up to 3 years after A day to register their funds.

Small pension funds - triviality

If the fund is less than 1% of the Lifetime Limit (i.e. £15,000 in 2005/06) when you come to draw the pension, you are able to draw the whole fund as a cash lump sum rather than purchase an income, but the amount of the small pension over the tax free cash allowance will be taxed to you as income.

Planning issues relating to ALL those with existing pensions

It is very important that those with existing pensions know how the new rules are going to affect them otherwise they may have problems in the future when it comes to drawing their pensions. Issues to be particularly aware of can be summarised as follows:

- EPP or SSAS where current tax free cash is greater than 25% of the fund – need to ensure you don't lose this benefit.
- High and uncompetitive charges on old funds.
- Poor performing investment funds.
- For policies over 20 years old – poor death benefits.
- Those wanting to draw benefits imminently who are currently between 47 and 53.

If you have any questions or need an independent review of your pension arrangements, please contact Martin Andrews to discuss your situation further. Martin Andrews & Associates Ltd is an Independent Financial Adviser authorised and regulated by the Financial Services Authority.

Information given in this document should not be taken as advice as it is intended for guidance only. If you wish to have an assessment of your own situation, you should contact the office for advice.