Technical update

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Hot topics

Budget 2016

In comparison to recent Budgets, there were only a small number of items directly relating to pensions in the Budget, on 16 March 2016, with the most significant items shown below.

The headline news relating to long-term savings was the launch of a new Lifetime ISA, or LISA as it is already being referred to. It will apply for those under 40 in April 2017 and could turn out to be a significant development in pensions. There are many in the pension industry who believe that its introduction could be the first step along the road to moving to a Pensions ISA model.

The Lifetime ISA shares some features which are very similar to pensions. It therefore seems plausible that, if it is a success, modifications could be made in future Budgets to provide even more similarities to pensions such as:

• Raising the contribution or age limits; and/or

• Allowing company-sponsored Lifetime ISAs to be used as an alternative to pensions for auto enrolment purposes.

The impact of this is that, potentially, we will see a decrease in membership of 'traditional' pension schemes amongst the under 40s, as people divert savings into Lifetime ISAs.

On the day of the Budget, the government also provided a response to the pensions tax relief consultation that had been launched at the Summer Budget in 2015. The most notable aspect of this was the lack of indication given by the government on its thoughts about how the tax treatment of pensions might develop.

A further pension-related development announced within the Budget documentation is that the government intends to work with the pensions industry to launch a pensions dashboard by 2019 to help individuals view all their retirement savings in one place. It is anticipated that there will be industry consultations on the development and funding of this.

As well as the above developments, the Budget announced measures relating to the provision of pensions advice:

• The government will consult on introducing a Pensions Advice Allowance, which will allow people to draw up to £500 tax free from their defined contribution pension pot for use against the cost of financial advice; and

• From April 2017, there will be an increase in the amount that can be spent by employers for

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pensions advice for its employees without incurring tax and National Insurance on the employee. The increase will be from £150 to £500 and may give those employers who offer pre-retirement seminars an opportunity to expand the scope of material delivered within them.

Prior to the Budget, there had been speculation that salary sacrifice for pensions would be abolished. Whilst the government is considering limiting the use of salary sacrifice, it stated its intention is that this should not affect the use of salary sacrifice for pension saving.

No new changes to the Lifetime Allowance or Annual Allowance were announced, although the Budget documentation confirmed that the proposed changes applying from 6 April 2016 will go ahead, which includes:

• The tapering down of the Annual Allowance from £40,000 to £10,000 for tax years from 2016/17, for those with both taxable income of over £110,000 and an adjusted income of over £150,000 for that tax year; and

• The Lifetime Allowance reduction from £1.25 million to £1 million (subject to transitional protections), with CPI-linking from April 2018.

Other developments

Pension liberation

The Pensions Regulator (tPR) has recently unveiled a refreshed scorpion campaign to warn of the dangers of pension scams. The campaign has been revamped to be clearer to savers and highlight the dangers imposed by pension scams.

tPR states that thousands of people have lost their life savings after falling for a pension scam. Some of the tactics used by pension scammers include offering free pension reviews, health checks and promises of better returns on their savings, pension loans, upfront cash or other promotions to tempt them.

Within the transfer process, RPMI carries out steps to warn members of the risks of pension scams and in establishing information about the potential receiving scheme, such as whether the member has been approached by the scheme via a cold call or text message. RPMI only complies with a member's request to transfer if it is to an arrangement which provides evidence that it is registered with HMRC or is an overseas scheme included on HMRC's list of Recognised Overseas Pension Schemes. Checks are also carried out on the receiving arrangement to establish whether it appears to be a bona fide pension arrangement.

Pension Protection Fund (PPF) levies – 2015/16 and 2016/17 years

The 2016/17 PPF levy will be based on information submitted in the Scheme Returns and updated information on the Pensions Regulator's on-line system Exchange. The deadlines for the 2016/17 levy year are as follows:

• Scheme returns (including any voluntary section 179 valuations) will need to be submitted by midnight on 31 March 2016;

• Any deficit-reduction contributions will need to be certified and submitted by 5pm on 29 April 2016; and

• Full block transfers that have taken place before 1 April 2016 will need to be certified and submitted by 5pm on 30 June 2016.

September 2015 inflation figure

The Office for National Statistics announced during October 2015 that the level of inflation as at September 2015, as measured by the Consumer Prices Index (CPI), was -0.1%. The corresponding level of inflation, as measured by the Retail Prices Index (RPI), was 0.8%.

The September CPI inflation figures are commonly used when setting the level of pension increases within the rules of many pension schemes.

In addition to this, the September inflation figures have the following impacts on pension schemes:

• The Notional Earnings Cap, originally introduced by the Finance Act 1989, is expected to increase from £149,400 to £150,600 from 6 April 2016, as this item continues to be adjusted in line with RPI inflation.

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• The calculations of Pension Input Amounts for Annual Allowance purposes for 2016/17 will not have any inflationary increases applied to benefits accrued prior to that tax year.

Background information

Reduction to the Lifetime Allowance

The Lifetime Allowance will reduce from £1.25 million to £1 million with effect from 6 April 2016, and will increase in line with inflation from 2018 onwards. The Lifetime Allowance is the total amount of pension savings that an individual can build up within registered pension schemes during their lifetime, and if it is exceeded tax is charged on any savings over the limit. Two types of protection are being made available by HM Revenue and Customs:

• Fixed Protection 2016 will allow an individual to retain a Lifetime Allowance of £1.25 million, although the individual must not accrue any benefits after 5 April 2016 to have this; and

• Individual Protection 2016 can provide an individual with a bespoke level of Lifetime Allowance where that individual has pension savings of at least £1 million on 5 April 2016.

Applications for Fixed Protection 2016 and/or Individual Protection 2016 can be made online from July 2016 and there will be no deadline for applications to register. However, any members who wish to use Fixed Protection will need to have opted out of active membership so that accrual of benefits within any defined benefit schemes ceases before 6 April 2016 and no contributions to defined contribution schemes are paid from that date. An interim process will allow members who want to take their benefits between 6 April 2016 and July 2016 to make a temporary application for protection.

Reduction to the Annual Allowance

The 2016 Budget confirmed the changes announced in the 2015 Summer Budget to the Annual Allowance for higher earners:

From 2016/17, those with 'adjusted income' over £150,000 will have their Annual Allowance reduced by £1 for every £2 of adjusted income over £150,000. The maximum reduction is £30,000. This is referred to as the tapered Annual Allowance.

As a consequence of the taper, individuals with adjusted income of £210,000 or more will have an Annual Allowance of £10,000.

For this purpose, 'adjusted income' is typically based on:

• An individual's taxable income; plus

• The level of that individual's pension savings, as measured by the pension input amount under Annual Allowance rules.

Typically, those with taxable income below £110,000 will not be subject to the new taper and will therefore retain an Annual Allowance of £40,000.

The fact that many members will have elements of non-pensionable pay or income from non-employment sources (e.g. income from personal assets such as property) means that there will be some members with pensionable pay considerably lower than £150,000 who are impacted by the tapered Annual Allowance.

Consequently, it is difficult to quantify how many members of pension schemes may be impacted by the tapered Annual Allowance, especially when there are material levels of non-pensionable earnings. Furthermore, for those members who are impacted by the tapered Annual Allowance, it is also difficult to quantify what reduced level of Annual Allowance will apply.

The government published draft legislation for consultation relating to the provision of pension savings statements to those who may exceed the Annual Allowance under the tapered Annual Allowance regime. This suggested that pension savings statements would be required for all those with 'pensionable earnings' of £110,000 or more, although it was unclear how 'pensionable earnings' was defined for this purpose. Following this consultation and comments that this would be overly-burdensome, changes were made to the legislation laid before Parliament on 9 March 2016 so that trustees will only be required to provide a pensions savings statement for the 2015/16 tax year if the full Annual Allowance is exceeded. However, it is not yet clear whether the legislation will be revisited for the provision of pension savings statements for 2016/17.

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In addition to the above changes, as part of the introduction of the tapered Annual Allowance, transitional measures have been in force for the 2015/16 year. The aims of these have been to:

• Align all pension input periods with the tax year by 5 April 2016; and

• Protect pension savings already made from any retrospective tax charges.

The transitional measures that were introduced:

• Resulted in a cessation of all pension input periods in progress on 8 July 2015 and the creation of a one-off pension input period between 9 July 2015 and 5 April 2016;

• Provide pension input periods ending within the 2015/16 year with a combined Annual Allowance of £80,000, reflecting the possibility that some individuals will have already used their Annual Allowance for a pension input period that was expected to end in the 2016/17 year; and

• Allow up to £40,000 of the above allowance to be within the pension period from 9 July 2015 to 5 April 2016.

These transitional measures also apply fully to members of schemes, where the pension input period was already aligned with the tax year.

State Pension reform and end of contracting-out

The two-tier system of basic State Pension and additional State Pension is replaced with a single-tier State Pension from April 2016.

Key aspects of the new system are:

• The single-tier pension, now referred to by the government as the new State Pension, will only apply to those reaching State Pension Age from 6 April 2016;

• The full level of the new State Pension will be around 30% higher than the equivalent basic State Pension, although transitional arrangements will mean that not everybody gets the full amount; and

• The ending of accrual of additional State Pension means that defined benefit pension schemes will no longer be able to be contracted-out.

The starting level of the new State Pension was announced as part of the government's Autumn Statement on 25 November 2015 and is £155.65 per week from April 2016. The basic State Pension is to be increased in accordance with the 'triple lock' formula, bringing it to £119.30 a week from April 2016.

The implementation of the new State Pension does not typically impact items within scheme rules which have explicitly used the basic State Pension within their calculation. Items like these will still be based on the basic State Pension and the basic State Pension will continue to be paid for those who had already reached State Pension Age by 5 April 2016.

The government has embarked on a marketing campaign to raise awareness about the State Pension changes.

Members over age 50 are now able to get a State Pension statement based on the new State Pension system. Details about how this can be obtained are available at www.gov.uk/state-pension-statement. There is also a State Pension age calculator on the same site. The first of the independent State Pension age reviews, scheduled for each Parliament, has recently been launched and will be led by John Cridland CBE, who is a former Director General of the Confederation of British Industry (CBI). The review will report to the government in time for it to announce recommendations by May 2017.

The government has dismissed calls for new transitional arrangements to be put in place for women hit particularly hard by State Pension equalisation and the increase in their State Pension age, despite MPs unanimously voting in favour of helping those women affected.

As a consequence of contracting-out ending, National Insurance contributions will be increased in respect of active members' earnings in a band between £5,824 and £40,040 per annum by:

• 1.4% for employees; and

• 3.4% for employers.

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In order to try and help sponsoring employers mitigate the extra costs resulting from the end of contracting-out, the government has given employers a statutory power to allow them to amend their schemes, although this power cannot be exercised for Protected persons. Regulations set out detail of how the statutory power may be used.

It was announced at the Autumn Statement in 2015 that legislation will be introduced, as part of the Finance Bill 2016, to allow bridging pensions to be aligned to the new State Pension.