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TAX SIMPLIFICATION – FURTHER CHANGES ANNOUNCED

1 BACKGROUND

The Inland Revenue has announced a further package of measures which will form part of the tax simplification changes due to come into force on 6 April 2006 (A-Day).

Many of the new measures stem from on-going "liaison" with the pensions industry following the enactment of the Finance Act 2004 ("2004 Act") in July of last year. The aim is to provide schemes and individuals with additional flexibility, to clarify certain aspects of the 2004 Act, to smooth the transition from the current to the new tax regime and to introduce "further anti-abuse and compliance rules".

The new measures cover four main areas of the current tax simplification proposals:

- benefits and contributions;
- lifetime allowance;
- unauthorised payments;
- transitional issues.

2 SOME EXAMPLES

Some examples of the new measures include:

2.1 **Definition of "dependant"** – this will be extended to include an individual who was married to the member when his/her pension first came into payment, but who is divorced from the member by the date of his/her death.

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Under the 2004 Act, a dependent child's pension (other than an incapacity pension) ceases to be payable at age 23. There will now be a transitional relaxation to allow a child's pension in payment at A-Day to continue (even if that child is over 23) until he or she finishes full-time education or vocational training.

2.2 **50 member rule** – the current proposal that schemes (including defined benefit arrangements) with fewer than 50 members must provide scheme pensions through an insurance company will be scrapped. The rule was designed as an anti-abuse measure and to protect members of smaller schemes. Further changes will be made to the 2004 Act to guard against "lump sum abuse" and the view now seems to be that member protections being introduced by the Department for Work and Pensions under the Pensions Act 2004 will suffice.

2.3 **Pensions in payment** – a relaxation will be made to allow pensions in payment to be reduced in certain circumstances (for example, where there is a pension sharing on divorce order).

2.4 **Lifetime allowance tax charge** – where this has been overpaid due to an error, a scheme administrator will be able to claim a repayment from the Inland Revenue. In some circumstances, this can then be used "to pay out benefits to the individual as if the error had not been made".

2.5 **Lump sums** – individuals with enhanced protection will be prevented from taking benefits in excess of the lifetime allowance as a lump sum (the general rule is that any excess over the lifetime allowance can be taken as a lump sum, subject to a 55% recovery charge).

2.6 **Funeral expenses** – "one-off tax free payments to be made upon the death of the member in order to fund funeral expenses…will not be authorised under the new regime if the member is aged 75 or over at death". But a transitional rule will permit such payments to

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continue to be paid tax-free "where a right to receive them exists (and the same right would have been offered if the member had joined the scheme on 10 December 2003) and the member has retired before 6 April 2006".

2.7 E-filing – registered pension schemes will be required to send Inland Revenue returns on-line and also to make payments electronically**.**

3 FINANCE ACT 2005

As the new measures will need to be incorporated into the 2004 Act, we can expect to see a reasonable proportion of the 2005 Finance Act dedicated to pensions. Whether any more changes will be added to the list remains to be seen.

In the meantime, for further details of the measures currently put forward, please see the Inland Revenue's website at:

http://www.inlandrevenue.gov.uk/pensionschemes/pensions-simplification-tn.pdf

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