Pensions tax changes from 6 April 2016

Alert | 23 March 2016

Introduction

While George Osborne's eighth Budget did not herald a major shift in the pensions tax relief system this time around (see our Alert for details), changes to the system are nevertheless on the horizon. On and from 6 April 2016, a number of these will come into force, including the introduction of the tapered AA and the reduction of the LTA to £1 million.

Key points

- From 6 April 2016, planned restrictions to the AA for higher earners will be introduced and the LTA will be reduced to £1 million.
- Transitional protections (Fixed Protection 2016 ("FP16") and Individual Protection 2016 ("IP16")) will be available for those with pension rights already at or around £1 million. While there is no deadline (as such) for applications, individuals who want to rely on either of these protections must apply to HMRC before taking any benefits on or after 6 April 2016.
- The requirement to provide certain members with a pension savings statement has been modified in respect of the 2015/16 tax year and individuals with income over £110,000 will be able to request a statement.
- Tax on lump sums paid in respect of individuals who die aged 75 and over will be payable at the recipient's marginal rate from the tax year 2016/17.

The tapered Annual Allowance

From 6 April 2016, pensions tax relief will be restricted for individuals with "adjusted income" (ie taxable earnings including pension savings but excluding charitable contributions) above £150,000. Under the taper, for every £2 of adjusted income over £150,000 an individual earns, that individual's AA will be reduced by £1, subject to a maximum reduction of £30,000. Therefore, anyone with adjusted income of £210,000 or more will have an AA of just £10,000.

Individuals with income at or below a "threshold income" of £110,000 will not be subject to the new taper. Threshold income comprises an individual's taxable earnings, with pension savings generally excluded except for certain salary sacrifice arrangements introduced on or after 9 July 2015 (the day after the Summer Budget).

Transitional measures

To facilitate the introduction of the taper, the period over which pension savings are measured for the purposes of testing against the AA, known as the "pension input period" (PIP), is being aligned to the tax year. Transitional rules are in place to protect pension savers from retrospective tax charges which might otherwise result from aligning PIPs in this way. For this purpose, the 2015/16 tax year has been spilt into two: "the pre-alignment tax year" (which runs from 6 April 2015 to 8 July 2015 inclusive) and "the post alignment tax year" (which runs from 9 July 2015 to 5 April 2016 inclusive).

Under the transitional provisions, for the 2015/16 tax year only, individuals will generally have an AA of between £40,000 to £80,000 inclusive. The transitional rules are complex and the exact amount of available AA will vary from individual to individual, depending on the amount of pension savings made in any PIP ending in the pre-alignment tax year.

The money purchase AA

Individuals who flexibly access their DC pension savings become subject to "the money purchase AA" where they make subsequent DC pension savings exceeding £10,000. If the individual exceeds the money purchase AA, the "alternative AA" of £30,000 will then apply in respect of any non-DC (DB) pension savings.

Where an individual is subject to both the new taper and the money purchase AA rules, his or her alternative AA will be reduced accordingly.

Information requirements

Where an individual's pension savings in any scheme exceed the AA in any given tax year, the scheme administrator (trustees) must provide the member with a pension savings statement informing them of this by 6 October following the end of that tax year. In respect of the 2015/16 tax year, trustees will be required to provide a pension savings statement to a member if either:

- their pension savings for the whole tax year exceeds £80,000
- their pension savings for the post-alignment tax year exceeds £40,000.

In addition, individuals with income of £110,000 or more will be able to request a statement but the trustees will not be required to provide one unless asked.

As the taper begins to bite, further changes to the information requirements are likely to be made.

The Lifetime Allowance

From 6 April 2016, the standard LTA will be reduced to £1 million from its current level of £1.25 million.

As with previous reductions in the LTA, protections will be available for those with pension rights at or around the £1 million mark. Individuals wanting to rely on either FP16 and / or IP16 must apply to HMRC before taking any benefits on or after 6 April 2016. However, in contrast to previous protections from the LTA, other than this there is no cut-off point (as such) for applying.

Individuals will be able to use an online self-service facility to apply for the new protections and will receive a reference number from HMRC. However, as the online system will not be available until July 2016, members wishing to take their benefits between 6 April 2016 and that date will need to write to HMRC informing it of their intention to rely on either or both of the new protections.

For more information about FP16 and IP16, please see our Alert.

Taxation of pensions at death

The tax rate which applies to certain lump sums paid on death is being amended from 6 April 2016.

Subject to certain conditions, lump sum death benefits can be paid free of tax from a registered pension scheme if the individual was under the age of 75 when they died. For example:

- such benefits are tested against the deceased member's LTA, so any excess could attract the LTA tax charge
- to qualify as an authorised payment and be payable free of tax charges, the lump sum must be paid at the trustees' discretion, within two years of the earlier of the date on which the scheme administrator (ie the trustees) first knew, or "could reasonably have been expected to know", of the member's death.

A tax charge of 45% currently applies in respect of lump sum death benefits where the individual dies aged 75 or over. From 6 April 2016, except in limited circumstances, tax will be payable at the recipient's marginal tax rate.

How we can help

For advice on dealing with any of the issues in this Alert, such as options for managing the new tapered AA, please speak to your usual Sackers' contact.

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