Finance (No.2) Bill 2023

Alert | 27 March 2023

Introduction

The Finance (No.2) Bill ("the Bill") was published today, 23 March 2023. With the notable exception of the abolition of the LTA, which is being dealt with by a separate Finance Bill, the Bill sets out measures which are intended to implement last week's Budget proposals.

Key points

As announced in last week's Budget, changes will be made to the pensions tax system so as to:

- increase the standard, money purchase and tapered AAs with effect from 6 April 2023
- remove the LTA charge with effect from 6 April 2023
- generally freeze the maximum PCLS at £268,275 (being 25% of the current LTA)
- grandfather existing rights to higher PCLSs for those with certain tax protections.

Annual allowance

The AA limits the total tax-relieved pension savings an individual can make each tax year across all registered pension schemes.

The Bill includes measures which, with effect from 6 April 2023, will:

- increase the standard AA from £40,000 to £60,000
- increase the money purchase AA (which applies to any subsequent DC savings by individuals who flexibly access their DC benefits) from £4,000 back up to its previous level of £10,000
- increase the minimum tapered AA from £4,000 to £10,000, and the threshold at which the taper applies from £240,000 to £260,000. The taper works by reducing the AA by £1 for every £2 of income over the taper threshold. This means that the minimum £10,000 taper will apply to individuals whose income is £360,000 or more.

Lifetime allowance

The LTA limits the total amount of tax-relieved pension savings that an individual can build up over their lifetime across all their registered pension schemes without incurring an additional tax charge.

With effect from 6 April 2023, the Bill will:

- remove the LTA charge
- ensure that certain lump sums which can currently be subject to an LTA charge of 55% (serious ill-health lump sums, LTA excess lump sums, DB lump sum death benefits and uncrystallised funds lump sum death benefits) will be taxed at the recipient's marginal rate.

With effect from 6 April 2024, the LTA will then be abolished altogether. Presumably to allow ample time to work through the substantial changes which will be required to pensions tax legislation, this will be the subject of a future Finance Bill.

Trustees and administrators should note that, as the LTA framework will remain in place until 6 April 2024, HMRC has confirmed that they will need to continue to operate LTA checks when paying benefits (for example, assessing whether an individual has available LTA) and to issue benefit crystallisation event statements.

LTA protections

When the current pensions tax regime came into force on 6 April 2006 (A-Day), measures were introduced for those whose benefits were already near or exceeded the new LTA. Since A-Day, the LTA has been reduced several times and, each time, additional protections have been put in place.

In the Budget, Jeremy Hunt, the Chancellor of the Exchequer, announced that, for those without protections, the pension commencement lump sum ("PCLS") will be retained at its current level of £268,275 (25% of the current LTA) and "will be frozen thereafter".

With effect from 6 April 2023, the Bill will ensure that members with protected lump sums, eg valid enhanced or fixed protection, will retain their entitlement to a higher PCLS.

Helpfully, HMRC has also confirmed that members who hold a valid enhanced or fixed protection will be able to accrue new pension benefits, join new arrangements or transfer their benefits from 6 April 2023 without losing this protection. To benefit from this, the relevant application must have been made before 15 March 2023.

Miscellaneous

The Bill will also:

- as promised in the Autumn Budget 2021, establish a new system for HMRC to make top-up payments to low earners contributing to "net pay" pension arrangements who do not receive the 20% tax relief which is automatically applied in "Relief at Source" pension arrangements. This change is intended to come into force from the 2024-25 tax year

- better accommodate collective defined contribution ("CDC") schemes within the existing pensions tax framework, by enabling CDC schemes in winding-up to continue to pay periodic income or transfer assets to pay a drawdown pension under another registered pension scheme

- ensure that any pension assets reclaimed by members from the Dormant Assets Scheme are taxed as if they were the original pension benefits.

Next steps

The Bill will now make its way through the Parliamentary process. We would expect it to receive Royal Assent before the summer recess.

In the meantime, trustees should consider whether to issue a communication to members, both to explain the proposals and to make clear that they are not yet set in stone. We recommend advising individuals to take independent financial advice before taking any action based on the Budget announcements. It is also worth bearing in mind that a change in the governing political party could result in further alterations, or a complete reversal of the current proposals.

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