

Defined Contribution Pensions and the 2014 Budget



Agenda

- **Introduction**
- **Pre-Budget Position**
- **Summary of Chancellor's announcement**
- **Immediate changes in effect from March 2014**
- **Proposed Outcome of announcement from April 2015**
- **Next Steps & Consultation**



Introduction

- **On March 19th the Chancellor, George Osborne delivered his budget**
- **In this he announced some radical proposed changes to pensions in the UK**
- **Some of these came into effect from 27th March 2014**
- **Some are proposed to be effective from April 2015**
- **Purpose of today to explain the content of the Budget**

Pre-Budget Position

Defined Contribution (DC) Pension

You accrue a fund dependant upon

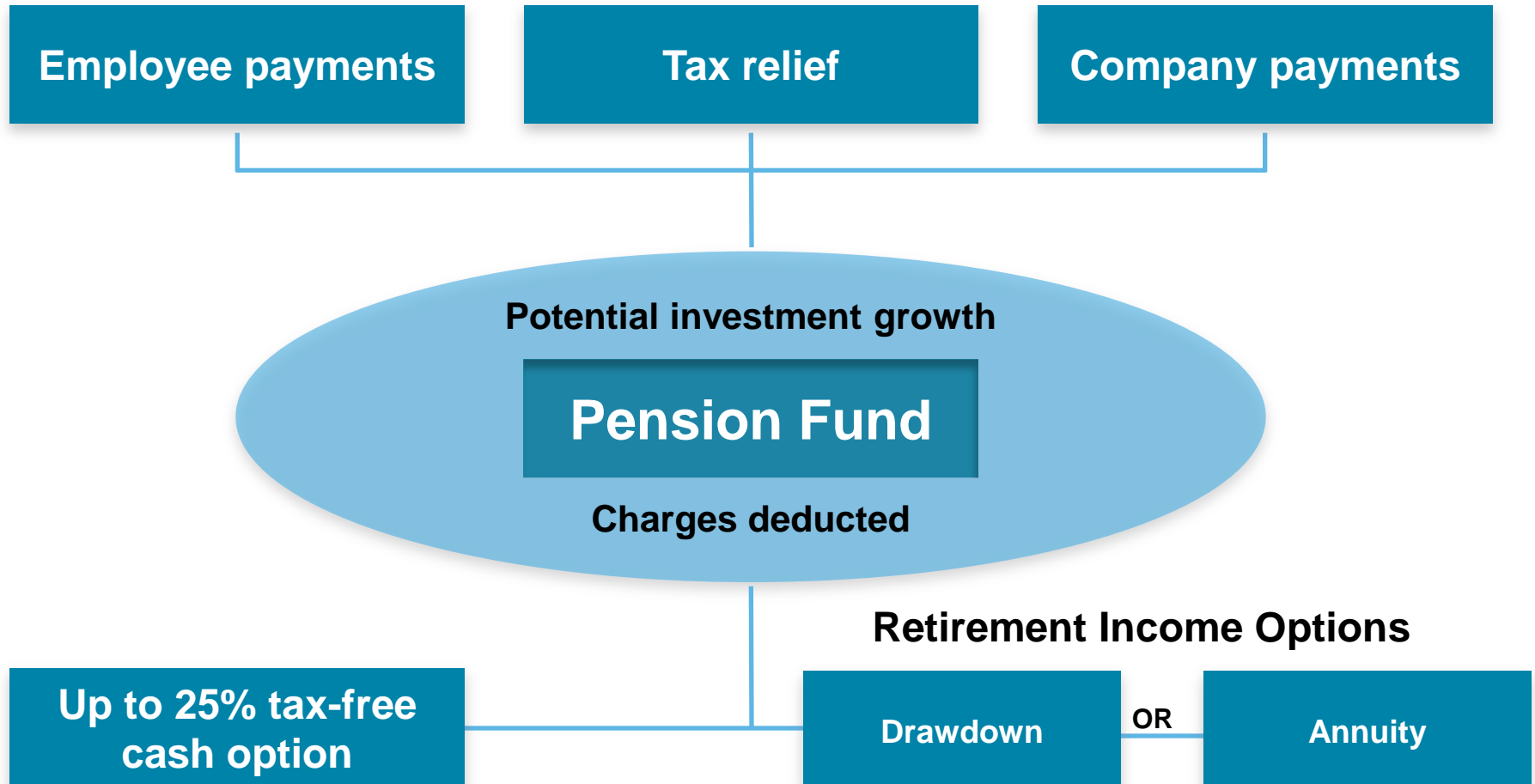
- Contributions
- Investment Return
- Charges levied

The value of the fund accrued dictates the value of the pension that will be paid in retirement subject to

- How you take your pension
- If you take a Lump Sum
- Benefits you want under your pension (such as spouses pension)



Pre-Budget Position continued....



Pre-Budget Position continued....

If aged over 60 further options at retirement:-

Trivial Commutation – If **all** pensions held total £18,000 or less there is an option to take the fund as a lump sum

(25% tax free, balanced taxed at marginal rate)

Small Pot Commutation – If an individual pension had a value less than £2,000 there is an option to take the fund as a lump sum irrespective of other pensions held. This can be done **twice** only.

(25% tax free, balanced taxed at marginal rate)

Current Retirement Options

- **Decision 1 – Do you take a Lump Sum (up to 25% of fund available)?**

This is tax free but will reduce the value of the fund you have to provide your income in retirement

- **Decision 2 – How do you take your retirement income?**

- **Option 1 – Buy an Annuity**

- **Option 2 – Use Pension Fund Withdrawal (PFW) also known as Drawdown)**



Annuity

- **An Annuity is an Insurance contract**
- **You use your fund to buy an income for life from an Insurance Company**
- **The amount you get will depend upon:-**
 - The value of your fund
 - Your Age
 - Where you live
 - What benefits you want e.g. Spouses benefit, increasing pension, Any guarantees, frequency of payment etc

Example of current Annuity rates

Based upon a non-smoker living in Poole with a fund of £100,000, with a spouse 3 years younger, payable monthly in arrears with a 5 year guarantee period

Age at retirement	Annual Level Pension	Annual Pension Increasing at 3% pa
55	£5,361.56	£3,319.56
60	£5,492.47	£3,527.40
65	£5,635.68	£3,696.72

Source: Money Advice Service Online quote service May 2014



Pension Fund Withdrawal

- Also known as Income Drawdown
- Pension Fund remains invested in a pension contract meaning Individual retains control & ownership
- Income drawn from the fund
- Government Actuaries Department (GAD) produce tables which calculate Maximum Levels of Income* permitted based upon
 - Age
 - Fund Size
 - Current Gilt Rate
- If you have lifetime pension income of £20,000 or more GAD limits are waived so no limit on income possible. This is called Minimum Income Requirements (MIR)

Pension Fund Withdrawal continued...

- Amount withdrawn can be altered each year to fit circumstances
- Fund remains invested so is subject to investment risk
- Positive investment return can increase funds and therefore possible income
- Negative investment return can erode fund and therefore possible income
- Needs to be reviewed on a regular basis to ensure correct investment strategy
- Maximum amount permitted reviewed every 3 years until age 75 and then Annually from Age 75

Examples of Income from Drawdown

Using the same example as for Annuity rates, namely non-smoker living in Poole with a fund of £100,000, with a spouse 3 years younger, payable monthly in arrears with a 5 year guarantee period

Age	Maximum Income permitted pa	Difference compared to Level Annuity
55	£5,760	+ £398.44
60	£6,360	+ £867.53
65	£7,080	+ £1,444.32

Source: Aon Hewitt - based upon March 2014 Gilt rate of 3.0%



Budget 2014

The Chancellor, George Osborne, announced radical changes to pensions in the UK with an aim to introduce greater freedom & flexibility for individuals in retirement

- Some of the changes came into effect the week after the budget – 27th March**
- Some are proposed to come into effect from April 2015 subject to current consultation**

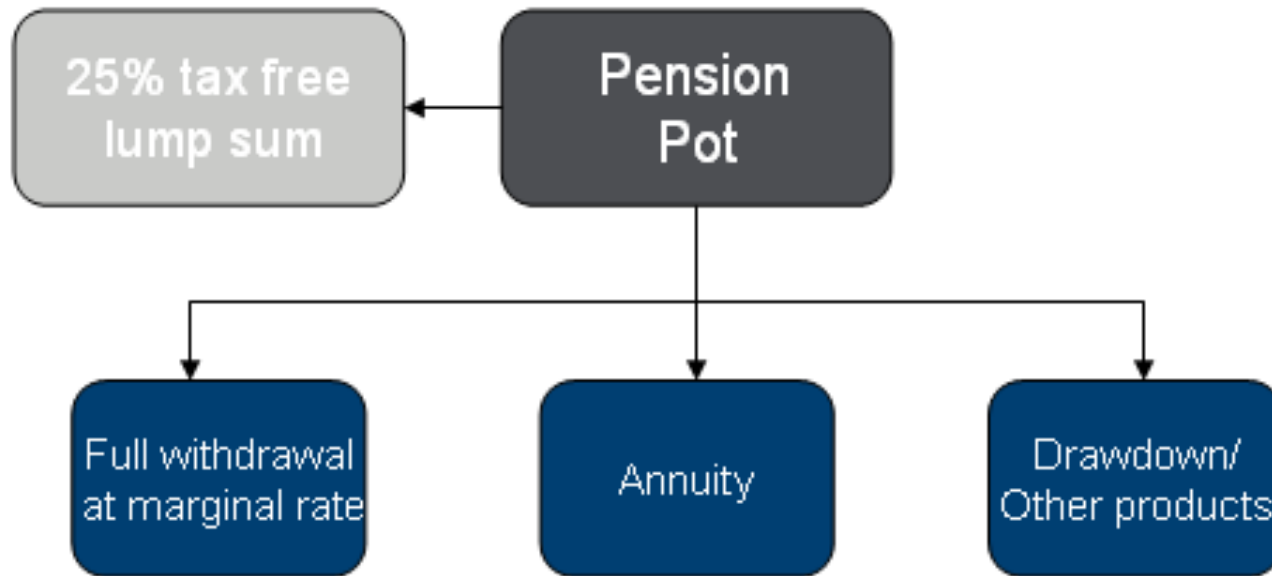
Immediate Changes

- **The Small Pot Commutation Limit will rise from £2,000 to £10,000 and can now be done three times**
- **The Trivial Commutation Limit will rise from £18,000 to £30,000**
- **The Minimum Income Requirement (MIR) will reduce to £12,000 meaning if you have guaranteed pension income (Annuity, State and/or scheme) there are no limits to the amount that can be withdrawn from DC fund via drawdown**



Proposed Changes from April 2015

- No compulsory annuitisation (but still an option)
- GAD limits on income from Drawdown removed
- Ability to withdraw entire fund at retirement (subject to tax)
- A ban on transfers from Public Sector Defined Benefit Schemes to DC Pensions



NB: These proposals are subject to Consultation which closes on 11th June 2014

What this means....

If the proposals are implemented..... You can use the entire pension fund as you wish

- **Tax Free Cash lump sum of up to 25% still available**
- **Still purchase an annuity**
- **Still utilise Drawdown but no limits on amount taken each year**
- **Withdraw the entire fund to invest/spend as you wish**

Advantages and Disadvantages - Annuity

Advantages	Disadvantages
Guaranteed income for Life	Need to select structure of annuity at time of purchase
No Investment Risk	Benefit ceases in event of death (or spouses death if they survive you)



Advantages and Disadvantages - Drawdown

Advantages	Disadvantages
Can amend income received to meet circumstances	Investment Risk on fund
Potential Investment Growth	Need for ongoing review
Ownership of Fund in event of death	Potential for fund to be eroded so doesn't guarantee you pension for life



Advantages and Disadvantages – Total Withdrawal of Fund

Advantages	Disadvantages
Can spend or invest as you wish*	No guarantee of income for life
Now truly a “savings plan”	Income Tax liability on 75% of fund which is added to income so could result in tax charge of up to 45%

* NB: Other investments utilised could give rise to further tax liabilities such as Capital Gains and Inheritance Tax liabilities



Next Steps in the process

- **Consultation will close on 11th June**
- **Matters considered**
- **Government will consider responses received**
- **Expected announcement of any amendments to the proposals by Q4 2014**
- **Implementation of amended proposals from April 2015**

Some of the matters to be considered

- A potential ban on transfers from all Defined Benefit Schemes to DC plans
- How the issues of taxation will be addressed?
- Can Pension Providers administer these new rules?
- Plus anything else raised by interested parties such as Consumer Groups, Pension Industry and Unions

*Based upon a 37 hour working week

Budget 2014

theguardian

Osborne's pensions 'freedom' will be a long-term social disaster

The chancellor's budget claims that making annuities optional is a great blow for freedom are far from the truth

 EXPRESS

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Final Thoughts

This is a radical overhaul of the pensions landscape which will give individuals greater scope and flexibility as to how they structure their retirement plans and income

However, making ill informed decisions could cost the individual greatly as a wrong decision could result in low income in retirement, a large tax bill or having to return to work!

These changes can be great but it is imperative that everyone understands the options and therefore individual engagement is paramount to the success of these proposals



Over to you...

Question Time!