Budget 2014 & Pension Flexibilities

Significance for Individuals with Money Purchase Arrangements

In his Budget on 19 March 2014, the Chancellor of the Exchequer announced significant changes to the way in which individuals with money purchase arrangements would be able to access their pension funds from 6 April 2015. These changes were introduced to increase freedom and choice for individuals with money purchase arrangements, thereby allowing them more flexibility in providing for their retirement.

The 'Taxation of Pensions Act 2014' gave rise to the changes, providing two new options for those individuals wishing to access their money purchase funds flexibly; namely, Uncrystallised Funds Pension Lumps Sums (UFPLS) and Flexi-Access Drawdown Funds (FADF).

From 6 April 2015 it has been possible for individuals to take money purchase benefits from their uncrystallised lump sums as either a single UFPLS or a series of UFPLS. 25% of each payment of a UFPLS is free of tax and the remaining 75% is treated as taxable income and taxed at the individual's marginal rate of tax. UFPLS are only payable if the individual has available lifetime allowance.

Any new drawdown funds established from 6 April 2015 are deemed to be FADFs from which no limits exist on the amount of withdrawals that can be made over whatever period of time an individual chooses. When an individual designates funds to be put into a FADF, up to 25% can be paid tax-free as a pension commencement lump sum (PCLS). Thereafter, any payments from the individual's FADF are taxable as a pension.

Any individuals who take advantage of the new flexibilities from 6 April 2023 have their future savings to money purchase arrangements capped at a £10,000 money purchase annual allowance (MPAA). This figure was £4,000 for tax years between 6 April 2017 and 5 April 2023. The MPAA is triggered as soon as an individual accesses savings flexibly for the first time, which includes receiving a UFPLS or a payment from a FADF.

Significance for Schemes with Money Purchase Arrangements

Schemes with money purchase benefits do not need to offer the full range of flexibility options to their members. However, a permissive scheme rules override allows trustees to make payments under the new flexibility rules without having to amend the scheme rules first. Should a scheme choose to not provide the full range of options, members will have the right to transfer their benefits to an alternative arrangement which does offer the full range of options.

Information Requirements

There are information requirements to ensure that individuals who have accessed their pension savings flexibly are aware of the tax consequences. To that end, within 31 days of an individual accessing his benefits flexibly, the Scheme Administrator must notify the individual that he is now subject to the MPAA of £10,000. This figure was £4,000 for tax years between 6 April 2017 and 5 April 2023. Furthermore, the Scheme Administrator must inform the individual that within 91 days he must report this to any other schemes to which he is contributing.

If an individual finds himself subject to the MPAA and has total pension input amounts in respect of his money purchase (or hybrid) arrangements of more than £10,000 (£4,000 for tax years between 6 April 2017 and 5 April 2023), the Scheme Administrator must provide the individual with a 'pension savings' statement and, additionally, notify HM Revenue & Customs of the individual's details and pension input amounts using the Event Report.

Miscellaneous Features of Taxation of Pensions Act 2014

The Taxation of Pensions Act 2014 additionally:

a) Reduced the age limit for taking trivial commutation and small pot lump sums from age 60 to 'normal' Minimum Pension Age (MPA), which is currently 55 but set to rise to State Pension Age (SPA) less 10 years from 6 April 2028 onwards

b) Amended the definition of a trivial commutation lump sum so that it no longer applies to money purchase arrangements (small pot lump sums continue to apply to defined benefit and money purchase arrangements)

c) Increased the maximum trivial commutation lump sum death benefit from £18,000 to £30,000 (in line with the maximum trivial commutation lump sum amount)

d) Extended the trivial commutation lump sum death benefit rules to allow the remainder of a guaranteed pension up to a value of £30,000 to be taken as a lump sum on death rather than continue to be paid as a pension

e) Increased the flexibility of the income drawdown rules for all 'new' FADFs from 6 April 2015 by removing both the maximum cap on withdrawals and the minimum income requirements

f) Enabled those individuals with 'capped drawdown' in force at 6 April 2015 to convert to a FADF

g) Removed the maximum 10 year guarantee period for lifetime annuities, thereby enabling annuities to continue to be paid after an individual's death

h) Allowed annuities to reduce (as well as increase) once in payment

i) Provided that where an individual becomes entitled to a lifetime annuity before the 'normal' MPA (unrelated to ill health) the amount treated as crystallised by that annuity at 'normal' MPA is to be the higher of twenty times the annual rate of the annuity and the original value of the assets used purchase the lifetime annuity

j) Restricted (or reduced) certain tax charges in relation to death benefits; particularly in so far as individuals have freedom to pass on their unused money purchase pension to 'any' nominated beneficiary when they die without having to pay a tax charge - (the Act also provided that persons other than dependants can be the recipients of unused drawdown funds, with two new categories being created: a 'nominee' of the scheme member and a 'successor' of the scheme member; the latter being an individual nominated by a dependant of the member, a nominee of the member, a successor of the member or the Scheme Administrator)

k) Amended the 'recycling' rules (aimed at preventing the exploitation of the pension tax rules by using the tax-free cash sum to make further tax-relieved contributions) by reducing to £7,500 (from 1% of the Lifetime Allowance) the minimum aggregate value of tax-free lump sums that can be paid to an individual within any 12 month period