

**Client Briefing Note**

On 17 December 2002, the Government published a Green Paper entitled "Working and Saving for Retirement". Simultaneously, the Inland Revenue published a paper entitled "Simplifying the Taxation of Pensions". Responses to the proposals are invited by 28 March 2003 and 11 April 2003 respectively. The proposals may be changed during the consultation process prior to inclusion in a White Paper to be debated in Parliament with a view to enactment prior to 6 April 2004 ("A-day"). The proposals affect individual pension arrangements and Occupational Pension Schemes ("OPSs"). Based on our current understanding, our financial planning recommendations prior to A-day, subject to individual advice for each client, are set out below together with a summary of the main proposals.

**1. Clients not subject to the earnings cap and not a member of an OPS should consider:**

maximising contributions and utilising any unused reliefs to increase the fund to establish a lifetime limit in excess of £1.4 million with a view to (a) remaining unvested to age 75 in certain limited circumstances or (b) proceeding with income drawdown or (c) purchasing an annuity (especially the 'Open Annuity').

**2. Clients subject to the earnings cap and not a member of an OPS should consider:**

continuing to maximise contributions and reviewing the situation after A-day if the higher contribution limits are introduced.

**3. Clients who are members of an OPS and not subject to the earnings cap should consider:**

maximising contributions (including salary sacrifice) and possibly transferring out if the transfer value is approaching or in excess of £1.4 million and/or if in serious ill health (to maximise death benefits).

**4. Clients who are members of an OPS and subject to the earnings cap should consider:**

staying in the OPS and maximising contributions (including salary sacrifice).

<b>Summary of Main Proposals</b>
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**General**

- (a) Replace the current eight pension regimes with one from a date suggested to be 6 April 2004;
- (b) Limit tax privileges to a lifetime pension fund of £1.4 million and an annual contribution limit of £200,000 (or earnings if lower) after A-day - both limits indexed thereafter;
- (c) Allow pension rights built up before A-day beyond the lifetime limit to be crystallised (registration must be within three years of A-day), protected and indexed;
- (d) Permit further contributions with tax relief after the lifetime limit of £1.4 million is reached;

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- (e) Introduce a recovery charge of one-third of the excess of the pension fund over the lifetime limit (£1.4 million or the registered amount if greater) before benefits can be drawn;
- (f) Tax due on excess funds to be accounted for through self assessment but paid from the pension fund;
- (g) Allow a lump sum of up to 25% of the value of the matured pension fund to be drawn tax free up to the lifetime limit (and taxable thereafter);
- (h) Abolish carry forward/carry back rules for Retirement Annuity Policies (“RAPs”) and carry back rules for Personal Pension Plans (“PPPs”);
- (j) Include contributions into defined contribution (“DC”) schemes and the increase in the value of defined benefit (“DB”) pension rights in the assessment of the annual limit;
- (k) Publish Inland Revenue actuarial tables to determine the capital value of DB pension benefits (including pensions in payment) for calculation of lifetime limit;
- (l) Allow contributions to OPSs and personal schemes at the same time;
- (m) Count National Insurance rebates for benefit limits, but not contribution limits.

**Drawing Benefits**

- (a) Allow schemes to stagger vesting up to age 75;
- (b) Require mandatory vesting of pension funds by age 75 to provide an income although no requirement to purchase an annuity at any age;
- (c) Replace current income drawdown rules as follows:
  - (i) maximum income calculation similar to now, but minimum reduced to £1 p.a.;
  - (ii) review at least every five years up to age 75 and annually thereafter;
- (d) Use remainder of pension fund (even if lifetime limit exceeded) to provide pension income when lump sum has been drawn;
- (e) Raise minimum benefit age from 50 to 55 by 2010;
- (f) Allow the drawing of benefits whilst continuing to work for same employer;
- (g) Continue provision for ill health pensions before age 55;
- (h) Introduce “limited period” and “capital protected” annuities.

**Death Benefits**

- (a) Make benefits on death before vesting consistent for all schemes;
- (b) Allow lump sum death benefits before vesting up to age 75 to be tax free up to the lifetime limit and subject to the recovery charge thereafter;
- (c) Allow lump sum death benefits after vesting up to age 75 to be no more than the value of the fund used to provide the pension income less pension payments paid less 35% tax charge (will not apply to people drawing income prior to A-day);
- (d) Allow taxable income benefits for survivors or dependants;
- (e) Include pension term assurance cover in the lifetime limit calculation;
- (f) Test funds providing death benefits against the lifetime limit.

This note is for general guidance only and represents our current understanding of law and Inland Revenue practice as at January 2003. We cannot assume legal liability for any errors or omissions and detailed advice should be taken before entering into any transaction. The value of investments and any income therefrom can go down as well as up and you may not get back the full amount you invested. Levels and bases of, and reliefs from, taxation are those currently applying but are subject to change and their value depends on the individual circumstances of the investor. For income drawdown policies, it should be noted that: high income withdrawals may not be sustainable during the deferral period; taking withdrawals may erode the capital value of the fund, especially if investment returns are poor and a high level of income is being taken – this could result in a lower income when the annuity is eventually purchased; annuity rates may be at a worse level when annuity purchase takes place and a certain investment return is required simply to “keep pace” with an annuity because a pension withdrawal or open annuity fund does not receive a benefit from the early death of other pensioners (‘mortality drag’) as does an annuity. Saunderson House Limited is regulated by the Financial Services Authority.