

Pensions Update – Changes from 6 April 2011

Questions and Answers – for existing Income Drawdown clients

Significant changes have been proposed which will affect pension regulations including income drawdown rules. These changes are due to come into effect on 6 April 2011, and could affect you and your pension plan.

We strongly recommend that you discuss these changes with your financial adviser to assess whether you are affected. The following questions and answers address the main issues and should help you in your discussion.

General

1. When do the changes come into effect?

The changes will come into effect on 6 April 2011, although you may not be immediately affected. For example, if you have recently commenced income drawdown or had your maximum income limit reviewed, you may not be affected for a number of years.

2. Do I have to purchase an annuity?

No. The requirement to purchase an annuity, at any age, has been abolished.

3. If I have a plan from which I have not taken benefits, what is the latest age by which I have to take benefits?

You do not have to take benefits from your plan, i.e. the previous age 75/77 threshold to take benefits will no longer apply.

4. If I have a plan from which I have not taken benefits, what is the latest age by which I can take a tax free lump sum?

You can take a tax free lump sum at any age, even if this is after age 75.

Income Drawdown

5. Is income drawdown changing?

Yes. From 6 April 2011 there will be two types of Drawdown Pension (income drawdown). The first will be known as “capped drawdown” and will operate in a similar manner to your current income drawdown plan with two notable exceptions. The second type of income drawdown is called “flexible drawdown” and will enable you to take all, or part, of your plan value as a taxed lump sum provided you have a minimum level of secure pension income. Please see questions 18 to 21. From 6 April 2011 we will refer to your income drawdown (Unsecured Pension) arrangement as your capped drawdown arrangement.

6. At what age does capped drawdown cease?

Capped drawdown will apply both before and after age 75 with no end age/date, i.e. this means you could remain in drawdown until death, whatever age that may be.

7. What will have happened to Alternatively Secured Pension (ASP) – current over age 75 drawdown?

ASP is to be abolished from 6 April 2011. All clients in ASP will become subject to the new capped drawdown rules.

8. What are the changes under capped drawdown?

- A reduction to the maximum drawdown limit from 120% to 100% of the 'basis' amount. The basis amount is the base calculation used to establish your maximum level of drawdown income payable from a pension fund. The basis value represents the yearly amount of annuity income your drawdown fund could purchase at the initial calculation and review points.
- An increase in the frequency of formal maximum income limit reviews. This means you will have your maximum capped drawdown limit reviewed every 3 years (instead of every 5 years) up until your 75th birthday. Thereafter, your maximum income limit will be reviewed every year.

9. Who will be affected by the changes?

Everyone who has an income drawdown plan will become subject to the new capped drawdown rules. However, the new maximum drawdown limit, and the new three yearly reviews applicable to capped drawdown, will only apply from the next formal review of your plan. In practice, this will be the earliest of the following events after 5 April 2011:

- The fifth anniversary of the most recent formal review;
- Following your 75th birthday: the first anniversary of the most recent review; or
- Following a transfer to another drawdown provider: the first anniversary of the most recent review.

If you are in income drawdown and between ages 75 and 77, the change to the new 100% maximum income limit will be made in respect of the drawdown year commencing immediately after the drawdown year which included 6 April 2011.

10. Will my maximum income limit change?

Yes – although this change should not affect your plan until the next formal review.

11. Since the maximum income limit percentage is changing, does this mean my actual maximum income will reduce?

The maximum income limit will reduce from 120% to 100% at your next formal review and this could result in a reduction to your maximum income limit.

12. Will my maximum income reduce on 6 April 2011?

No. Your maximum income limit should not, normally, change until the next formal review of your plan.

13. What factors will affect my maximum income limit at the next review?

When your maximum income limit is reviewed, a number of factors affect the new limit including the value of your plan at the time of the review (this takes into account the level of income you have previously been taking), your age and gender, and the income tables produced by the Government Actuary's Department (GAD) which are used to calculate your maximum income limit.

14. Will the Government be changing the GAD income tables?

Yes. New tables will be in use by 6 June 2011 at the latest. Depending on your age, there is likely to be a reduction in the income value.

15. Will my plan be reviewed immediately?

No. The switch to a 3 year review basis will not take place until after your next formal review.

16. Can I change my income year?

If you are under age 75 - no. However, if you are 75 or over and have more than one arrangement under the same scheme, it may be possible to change your income year.

17. How is my income year changed?

From age 75, your maximum capped drawdown is calculated annually for each of your arrangements. You can change the income year for an arrangement by asking us to change it so that it matches the income year of another arrangement you have under the scheme. The income year for an arrangement is changed by bringing the current income year to an end early. You cannot increase the length of an income year. The maximum capped drawdown will remain the same for the income year, even though it is shorter than usual.

Although you can change your arrangements to have the same income years, the maximum capped drawdown calculations are still carried out separately. The limit on your capped drawdown still applies per arrangement, not to the whole scheme.

You can only change the income year for an arrangement once.

18. What is “flexible drawdown”?

Provided you can meet the Minimum Income Requirement (MIR) of a “secure pension income” of at least £20,000 pa, flexible drawdown is available. If you satisfy the MIR, you may elect to take the whole, or part, of your plan as a lump sum subject to marginal rate of tax, i.e. basic plus higher rate tax, where applicable. A Scheme Administrator does not have to offer flexible drawdown and Alico will, at its discretion, consider flexible drawdown requests.

19. What counts as MIR?

MIR has to be a “secure pension income”, i.e. either a Lifetime Annuity or a Scheme Pension, as well as any State Pension you may receive. Capped drawdown income does **not** count as secure income.

20. Are there other conditions to be satisfied for flexible drawdown?

Yes. You need to have ceased all pension contributions and/or pension build up in any scheme. You will also need to sign a declaration confirming that you satisfy the MIR and provide confirmation of your “secure pension income”.

21. Can Protected Rights be taken as flexible drawdown?

No. Protected Rights cannot be taken as flexible drawdown until April 2012.

Triviality

22. What is a trivial commutation lump sum?

The encashment of small policy values. If your total pension savings from all of your pension schemes (excluding any State pension) is £18,000 or less, your fund can be paid as a trivial commutation lump sum. If you have not previously taken any benefits, 25% of the fund would be tax free and the remainder would be paid subject to basic rate tax. To request a triviality commutation lump sum, you need to be at least age 60 or older. If you wish to commute funds from more than one scheme/policy, you must do so within a specified 12 month period. You can only have one 12-month commutation period and once that period has passed, no further trivial commutation lump sum payments can be made.

Death benefits

23. If I am in serious (terminal) ill health, can I take my plan fund as a lump sum?

Yes. If you are under 75 when serious (terminal) ill health is paid, your plan fund can be paid as a tax free lump sum. If this occurs when you are aged 75 or above, there is a 55% tax charge deducted from the plan fund.

24. What lump sum death benefits are payable?

The death benefit paid from your plan depends on your age at the date of death, whether you have already started to take benefits and if you have any dependants.

- If you have not taken any benefits and are under age 75 at the date of death, there is no tax charge payable.
- If you have not taken any benefits and are over age 74 at the date of death, there is a 55% tax charge.
- If you have taken benefits and are in drawdown, there is a 55% tax charge.

If you have a spouse or registered civil partner, a Protected Rights fund will be used to provide them with an income. This requirement will cease in April 2012 – please refer to the first item under the Advance Notice of further changes on the last page.

25. If my plan fund is used to provide a dependant's income, will the 55% tax charge apply?

No. There will be no 55% tax charge if the death benefit used to provide a dependant's pension.

Contributions and the Annual Allowance

26. Is the Annual Allowance changing?

Yes. The Annual Allowance is the maximum amount that an individual (and/or their employer) may contribute towards an individual's pension in any one tax year and receive tax relief on the contribution paid – subject to the maximum personal contribution limit relating to your income. The Annual Allowance will be reduced from £255,000 to £50,000.

27. Can I contribute to my plan after age 74?

Yes. However, tax relief will not be granted on contributions paid into a plan after age 74.

28. Is 'carry forward' permitted?

Yes. Carry forward will be introduced and will apply if you do not use the whole of your Annual Allowance each year. Unused relief will be automatically carried forward for up to three years. Carry forward will be offset against any Annual Allowance tax charge, starting with the tax years 2008-09, 2009-10 and 2010-11 based on the assumed Annual Allowance of £50,000. There are a number of other conditions to be met to successfully 'carry forward' unused relief.

29. Are there exemptions to the Annual Allowance test?

The Annual Allowance test does not apply in the year of death. However, the "last year" exemption has been removed and this means that where previously you would have been able to contribute unlimited amounts in the year you took all of your benefits, the contributions will be subject to the Annual Allowance as normal.

Care

The above is a brief summary of the main changes coming into effect 6 April 2011. However, a number of the above areas have significant detailed conditions which this Question and Answer sheet does not cover. If you have any questions, please contact your financial adviser in the first instance or contact our Pensions Customer Services Team on 0800 013 2292 or email us at retirement@alico.com.

This leaflet is based on Alico's understanding of the proposals contained in the Finance Bill 2011 that will not become law until the Finance Act is passed. Any revisions, exclusions or additions made to the Finance Act prior to it being passed may affect the content of this Guide. The Advance Notice of further changes coming into effect in April 2012 has been drawn from a number of government department sources.



Advance Notice of further changes coming into effect in April 2012

The following are further changes due to come into effect on 6 April 2012:

- Money purchase contracting out (including via a personal pension) is to cease – so there will be no more Protected Rights / Non Protected Rights differentiation.
- The Lifetime Allowance will be reducing to £1.5m (from £1.8m).
- New “transitional protection” will be introduced for existing clients with funds between £1.5m and £1.8m who would be caught by the reduction in the Lifetime Allowance.
- Changes to triviality – current triviality is allowed if the aggregate value of a person’s pension fund(s) (excluding State pensions) is less than 1% of the Lifetime Allowance. Since the Lifetime Allowance is to reduce, the triviality limit will become a fixed monetary limit of £18,000.