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PENSION FREEDOM

The most radical reforms this century

In Budget 2014, Chancellor George Osborne promised greater pension freedom from April 2015. People will be able to access as much or as little of their defined contribution pension as they want and pass on their hard-earned pensions to their families tax-free. For some people, an annuity may still be the right option, whereas others might want to take their whole tax-free lump sum and convert the rest to drawdown.

EXTENDED CHOICES

'We've extended the choices even further by offering people the option of taking a number of smaller lump sums, instead of one single big lump sum,' Mr Osborne said.

From 6 April 2015, people will be allowed full freedom to access their pension savings at retirement. Pension Freedom Day, as it has been named, is the day that savers can access their pension savings when they want. Each time they do, 25% of what they take out will be tax-free. Under current rules, a 25% withdrawal must be taken as a single lump sum on retirement to be free of tax.

FREE TO CHOOSE

Mr Osborne said, 'People who have worked hard and saved all their lives should be free to choose what they do with their money, and that freedom is central to our long-term economic plan.'

From 6 April 2015, people aged 55 and over can access all or some of their pension without any of the tax restrictions that currently apply. The pension company can choose to offer this freedom to access money, but it does not have to do so.

ACCESSING MONEY

It will be important to obtain professional advice to ensure that you access your money safely, without unnecessary costs and a potential tax bill.

Generally, most companies will allow you to take the full amount out in one go. You can access the first 25% of your pension fund tax-free. The remainder is added to your income for the year, to be taxed at your marginal income tax rate.

This means a non–tax payer could pay 20% or even 40% tax on some of their withdrawal, and basic rate taxpayers might easily slip into a higher rate tax band. For those earning closer to £100,000, they could lose their personal allowance and be subject to a 60% marginal tax charge.

POTENTIAL TAX BILL

If appropriate, it may be more tax-efficient to withdraw the money over a number of years to minimise a potential tax bill. If your pension provider is uncooperative because the contract does not permit this facility, you may want to consider moving pension providers.

You need to prepare and start early to assess your own financial situation. Some providers may take months to process pension transfers, so you'll need time to do your research.

QUESTIONS TO ASK

It's important to ask yourself some important questions. Are there any penalties for taking the money early? Are these worth paying for or can they be avoided by waiting? Are there any special benefits such as a higher tax-free cash entitlement or guaranteed annuity rates that would be worth keeping?

If you decide, after receiving professional advice, that moving providers is the right thing to do, then we can help you search the market for a provider who will allow flexible access.

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Importantly, it's not all about the process. You also need to think about the end results.

WITHDRAWING MONEY

What do you want to do with the money once you've withdrawn it? You may have earmarked some to spend on a treat, but most people want to keep the money saved for their retirement. Paying off debt is usually a good idea.

If you plan just to put the money in the bank, you must remember you will be taxed on the interest. With returns on cash at paltry levels, you might be better keeping it in a pension until you need to spend it. Furthermore, this may also save on inheritance tax.

Finally, expect queues in April 2015. There's likely to be a backlog of people who've put off doing anything with their pension monies since last year. Those who get through the process quickly and efficiently will be the ones who've done the groundwork.

PROFESSIONAL FINANCIAL ADVICE YOU CAN TRUST

The contents of the Taxation of Pensions Bill, published on 14 October 2014 and dealing with pension reforms, are the most radical this century and are likely to affect everyone. There is a lot to think about, and you should obtain professional advice sooner rather than later to check how these reforms may impact on your particular situation. To discuss your requirements or for further information, please contact us – we look forward to hearing from you.