Pension News

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Pension allowance breaches surge

Data from HMRC has revealed a **significant increase** in the total value of pension contributions exceeding the Annual Allowance. It seems an increasing number of **people are falling foul of the overly complex rules and regulations.**

The most recent personal pension statistics, covering the 2017-18 tax year, show an astonishing 26,550 people reported contributions exceeding the £40,000 Annual Allowance in their self-assessment tax return, with combined total contributions amounting to £812m. That represents an average of £30,584 per person. Furthermore, over the past decade, the number of individuals reporting such a breach has risen dramatically, from £578 million in 2016-17 and £143 million in 2015-16. In addition, just 230 people faced similar tax charges in 2007-08 when the Annual Allowance was £225,000.

Pension complexity confounds the problem

The sharp rise in breaches can be primarily attributed to the sizable reduction in the Annual Allowance in 2011 and the introduction of the tapered Annual Allowance in 2016, which added greater complexity to the pension landscape. For higher earners, an additional taper brings the allowance down further to just £10,000 for individuals with total earnings of £210,000 or more.

Unless the government heeds industry advice and significantly simplifies allowance rules, the next few years are likely to see even more people caught out by this complex regime.

Change on the horizon

In its manifesto, the Conservative Party promised a review of the problem 'within the first 30 days'. In the Budget on 11 March, the newly appointed Chancellor Rishi Sunak, addressed the tapered Annual Allowance issue, which has caused problems for many key services, particularly impacting some senior high-earning NHS clinicians who are facing substantial tax bills if they and their employer pay into a pension above the tapered Annual Allowance. This has resulted in some key workers selecting to decline overtime to avoid a pension tax charge.

To support the delivery of public services, particularly in the NHS, the two tapered Annual Allowance thresholds for pensions have been raised by £90,000. The threshold income is £200,000, meaning individuals with income below this will not be affected by the tapered Annual Allowance and the Annual Allowance will only begin to taper down for individuals who also have an adjusted income above £240,000.

For very high earners the minimum level to which the Annual Allowance can taper down has reduced from £10,000 to £4,000 from April 2020. This reduction will only affect individuals with total income over £300,000.

Here to help

As many more people are discovering, a breach of allowances can be extremely costly. It is therefore vital to seek professional advice if you are unsure how pension allowances impact on you.

A pension is a long-term investment. The fund value may fluctuate and can go down. Your eventual income may depend on the size of the fund at retirement, future interest rates and tax legislation

Pension planning for the self-employed

There are 4.8 million self-employed people in the UK and only a third have any kind of pension arrangement. A shocking statistic when you consider that State support is shrinking and we're all living longer. Saving for a pension when you're self-employed is not as straightforward as it is for an employed person, who might automatically benefit from a workplace scheme and employer contributions. We've outlined some key points for you to consider.

Don't rely on the State Pension

Whether you're employed or self-employed you're entitled to the full basic State Pension (currently £168.60 a week) if you've paid in 30 years of National Insurance Contributions. If you're self-employed you can only claim the additional State Pension if you've had periods of employment. On its own State support is unlikely to enable you to continue your current standard of living into retirement. That's why it's imperative for the self-employed to find other ways to provide the additional income needed in retirement.

Start saving early

It's stating the obvious, but the sooner you start saving into a pension the bigger your potential retirement fund. You'll also have more time to benefit from the tax relief that's available.

To highlight the importance of saving early, a 25-year-old male looking to retire at 68 would need to contribute £236.25 per month in order to achieve a retirement income of £17,500 a year. If the same man had waited until he was 45 before he started saving, he would need to contribute £495.83 to achieve the same level of income, an additional £259.58 per month.

Minimise the amount of tax you pay

One of the main benefits of paying into a pension is the tax relief the savings attract. For example, if you're a basic rate taxpayer and pay £80 into your pension you effectively end up with £100 to invest. The maximum amount you can save each year that attracts tax relief (otherwise known as the annual allowance) is £40,000. Importantly, if your income is low and you're not able to save the full £40,000 in one tax year, you can carry forward any unused allowance, and use it towards contributions in the next tax year.

Please note:

- You must have been a member of a registered pension scheme during the years you want to carry forward
- Your tax relief is limited by your annual earnings in the year you want to carry forward
- You can only carry forward unused allowance from the three previous tax years

What type of pension is right?

The self-employed can choose from a range of different pension products, including stakeholder pensions, personal pensions and Self Invested Personal Pensions (SIPPs). Each has its advantages and disadvantages – we can advise on which is best for you.

HM Revenue and Customs practice and the law relating to taxation are complex and subject to individual circumstances and changes, which cannot be foreseen.

The value of investments and any income from them can fall as well as rise and you may not get back the original amount invested.

OW2489 Exp. 03/04/20

The factors influencing your pension choices

Planning the best way to draw your pension savings is not straightforward, after all, there's no 'one size fits all' when it comes to retirement.

Life expectancy, the impact of inflation and the choices available at retirement (thanks to the 2015 Pension Freedoms) are all influencing factors in your decision making. You'll also need to take into account not just your pension savings but any other investments or assets you might have.

Your pension choices

If you're aged 55 or over and in a defined contribution pension plan from 6 April 2015, you may be able to access your pension savings in a number of different ways:

- Buy an annuity
- Flexi Access Drawdown
- Uncrystallised Funds Pension Lump Sum (UFPLS)

If you decide not to purchase (or defer the purchase of) an annuity and instead take income using Flexi-access drawdown or UFPLS, adopting the right investment approach and keeping it regularly under review will be all important.

A question of balance

Balancing the potentially conflicting needs of income production and capital preservation is vital. Equally important is an understanding that personal circumstances will change throughout your retirement.

The three 'stages' of retirement

The early years
You're more active and therefore might want flexibility over how you draw your income.

The middle years
You're getting slightly less active and your lifestyle has settled into a more stable routine, so you'll need a more stable income level.

The later years
You may need to increase your income to cover, for example, the cost of care.

In all cases, investing and withdrawing in a way that aims to maximise the available tax benefits and minimise tax 'leakage'could help make your objectives easier to achieve. If you have some decisions to make about accessing your savings and, whether and how to continue to invest, it might help to consider:

- The extent to which you would like to leave an inheritance for your family and dependants
- Gifts - either now or in the future.
- Your current essential income needs such as your day-to-day living expenses and other "known/planned" expenditure.
- Your lifestyle and other "non-essential" expenditure such as holidays, new cars, sports and hobbies, entertainment etc.
- Unexpected items such as car repairs, home maintenance and health problems.
- Your current health status
- Future possible anticipated living expenses incorporating, possibly, a budget for care.

If you'd like advice on how you can make more of your investments and pension savings in retirement, or you'd like to find out more about pension death benefits, please get in touch.

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OW2113 Exp. 26/06/20