

Pre Budget Report (PBR) 2008 (For Professional Adviser Use Only)



Rumbles on the Jungle drums – has pension saving been dealt a low blow by the PBR?

Although many of the measures unveiled as part of the Pre Budget report were widely anticipated (and leaked), there were nonetheless some big surprises for the pensions sector. Undoubtedly there are some valuable short term gains and opportunities, however that said, there is a real sting in the tail. Like the budget itself, it is very much a picture of jam today, last Christmas' boiled sprouts tomorrow.

Float like a butterfly – the winners and gains

On the face of it, there is some cheer for both private and corporate pension investors alike.

i. Negative RPI can be positive

The government is projecting negative RPI during the course of 2009, which will provide much welcome relief for defined benefit pension schemes making pension payments and revaluing benefits in deferment.

It will also provide some respite for the Pension Protection Fund (PPF), whose funding margins have come under similar pressures. Although with the value of the FTSE having been slashed by nearly a third over the last few months, the temptation to increase the PPF levy will remain high.

ii. State pensioners not in so much of a state

For state pensioners and those on fixed income the news is equally good. State pensioners will see a one off payment of £60 in January which is the equivalent of having the rise due in April brought forward.

Plus, the standard minimum income guarantee in Pension Credit will see an above indexation increase, rising by £5.95 to £130 a week for single pensioners and by £9.10 to £198.45 a week for pensioner couples.

As the rise in state pension is fixed at the higher of 2.5% or RPI, and the RPI measure was taken in September (when RPI was its highest), it should mean that state pensioners and those on fixed incomes should see a slight increase in spending power.

iii. National Insurance rise remittance opportunity

One of the headlines grabbing the most column inches is the across the board 0.5% rise in National Insurance contributions from April 2011. NI contributions, unlike income tax, are extremely hard to mitigate as few concessions are granted.

However, one such concession is salary and bonus sacrifice, and the rise in NI contributions should make these arrangements far more valuable to both employees and employers.

This is particularly so as, although salary sacrifice affects State Second Pension benefits, in the longer term, State Second Pension will become a flat rate scheme offering far less benefits for those earning over £40,000. Therefore, although those earning over £40K will be paying more NI, they will not see any additional benefit in their state pensions.

iv. Tax rises signal increase in tax planning opportunities

Another of the biggest headlines was the decision to reduce the income tax personal allowance for those individuals earning in excess of £100k, and to introduce a 45% top tier of taxation for those with remuneration of £150k or above from April 2011.

This obviously creates the opportunity to offset part of the pain of these measures through increased pension contributions. This is particularly so for those caught by the £100k trap, who will see their marginal rate of taxation increase slightly.

v. VAT reduction gives temporary boost to SIPPs

The reduction of VAT from 17.5 pc to 15 pc will reduce the charges paid to large numbers of Self Invested Personal Pensions (SIPPs). The reduction equally applies to charges incurred from holding commercial property, such as those levied by external property managers and surveyors. This may make SIPP investments slightly more attractive to those who have formerly been concerned about the costs. However, it is worth remembering the reduction is probably only going to be temporary.

Sting like a bee – the losers and challenges

The predicted heist on Qualifying Recognised Overseas Pension Schemes did not materialise. Nevertheless, the PBR provides some very real longer term threats to those individuals who have larger pension pots, or have fully utilised the Annual Allowance.

i. Open Market Option Crackdown Update

The government also signalled that it wishes to keep Open Market Options (OMOs) at the top of the political agenda by announcing that it was shortly going to publish an update on the review of the operation of the OMO. The report will detail the progress made against the recommendations made as part of the 2007 PBR.

ii. No means to an end

The rise in Pensions Credit indicates that the government is still wedded to the idea of means tested pension benefits. This could act as a disincentive to save, and tax hardest the very people they are looking to attract to their Personal Account scheme. The above inflation rise will ultimately cause yet more people to be caught up in means tested benefits.

iii The big freeze – Lifetime and Annual Allowances to remain static for 5 years

It won't get many headlines in the paper, but the big pensions news is the announcement that the Lifetime Allowance and the Annual Allowance will remain frozen at their 2010 level for 5 years (i.e. to 2015). As a consequence, the effect of the Lifetime Allowance tax privileged cap will trickle down the pay scale much faster than had previously been anticipated, and could be particularly damaging if there is a period of high inflation before the next quinquennial review.

The restriction of the personal allowance, and extra tier of taxation, opens up tax mitigation opportunities for pension contributions, and higher tax relief. The constricted Lifetime Allowance means that only those that have lower levels of existing pension provision will probably be able to fully exploit them.

In essence the government move will prompt the need for many high net worth individuals to reassess their pension planning approach, particularly if they are within 5-7 years from retirement, and had based their previous strategy on the assumption that there would be rises in the Lifetime Allowance post 2010.

Finally, it also reinforces the need for those that are eligible to do so, to apply for transitional protection for the Lifetime Allowance charges before the deadline of 6 April 2009.

Summary

Planning Considerations

- Tax planning points for high net worth clients earning in excess of £100K
- Corporate tax planning issues for corporate clients in considering the value of using salary and bonus sacrifice alongside workplace pension schemes
- Pension planning points for those with large pension pots projected to be near or at £1.8m in 2010
- Pension planning considerations for those individuals who are making large pension contributions at or near the Annual Allowance



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