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2016 Pension Changes

Below is a brief summary of the potential changes that could come into force following the budget in March 2016. This information is based on our current understanding of the potential changes and should not be construed as advice. If you are in any doubt about how these changes might affect you then we strongly recommend that you seek independent financial advice.

1. Pension tax relief changes

Currently tax relief is available on pension contributions at your marginal income tax rate, up to a maximum of £40,000 in the current tax year where you have sufficient earnings.

The Chancellor has signalled his intention to change this in his forthcoming Budget on 16 March 2016, with the suggestion that a standard rate of relief will be applied to all pensions regardless of an individual's income tax rate. The new rate could be between 25% and 33%. This could mean an increase in tax relief for basic rate tax payers, but for higher and additional rate tax payers it would reduce the tax relief benefit so the total gross contribution going into the pension would be less.

What you need to consider?
There is no certainty about what the change will be, or when it might be applied. If you are concerned that you might be affected by a reduction in tax relief you should seek advice from an FCA regulated financial adviser. You must bear in mind that whatever decision you make, should you contribute more than the Annual Allowance (taking into account any 'carry forward' availability) the tax relief you have received can be reclaimed by HMRC through a tax charge.

2. Changes to the Annual Allowance (AA)

The annual allowance is the maximum amount that can be contributed to your pension in any one year and still receive tax relief (this includes employer and any other third party contributions). Currently the AA stands at £40,000, but you can also 'carry forward' any unused AA from the past 3 years, including the 'double allowance' resulting from changes to the current (2015/16) allowance.

For individuals whose income is more than £150,000 (including employer contributions into their pension and other non-personal contributions), or whose income is more than £110,000 excluding pension contributions, the annual allowance will be reduced. The reduction is £1 for every £2 of income over £150,000, subject to a maximum deduction of £30,000, i.e. leaving you with an annual allowance of £10,000.

Example

Your income is £130,000 and your employer pays a further £30,000 into your pension.
Therefore your total 'adjusted income' is £160,000
This is £10,000 over the £150,000 limit
So your new AA would be:
£10,000/2 = £5,000
£40,000 - £5,000 = £35,000 (the original AA minus the deduction)
So your new annual allowance would be £35,000

'Anti-avoidance' measures will apply so that any salary sacrifice arrangement set up on or after 9 July 2015 will be included in these calculations.

Please note: contributions above your available allowance may incur a tax charge at your marginal rate.

What you need to consider?
Before 6 April 2016 you still have the opportunity to use the full annual allowance - and any unused allowance from the last 3 tax years, including the 2015/16 'double allowance'. You can read more about 'carry forward' in our ‘Contributions into SIPP Guidance notes’ that can be found on our website.

3. Reduction in the Lifetime Allowance from 6 April 2016

Also announced in the 2015 Summer Budget, from 6 April 2016 the Lifetime Allowance (LTA) will reduce from £1.25m to £1m. The LTA is calculated on the total value of all your pensions, both employer and personal. This value is measured at the point at which you start to draw on your pension (or at various other times such as at age 75) and includes investment growth and income.

Should you exceed the LTA, you can either take the excess as a lump sum, subject to a 55% charge OR keep it in your pension less a charge of 25%. Income from that pension is then taxable at your marginal rate.

What you need to consider?
If you have not previously arranged protection following previous changes to the LTA, you can apply for 'lifetime allowance protection 2016'.

There are two types of protection available:

Fixed protection 2016 – you retain an LTA of £1.25m but cannot make any further pension contributions after 5 April 2016. Should you make any further contributions this would re-set your LTA to £1m (investment income and growth does not count as a contribution.)

Individual protection 2016 – this will be available for anyone with a current fund value of over £1m as at 5 April 2016. The protection protects the value of the fund up to £1.25m. Further contributions can still be made.

It is your own responsibility to apply for protection before 6 April 2016. To apply for either protection scheme you will need to write to HMRC.

You can learn more about the lifetime allowance changes and applying for protection on HMRC's website.