Institute and Faculty of Actuaries

Ian Hook
Senior Executive Officer
Scrutiny Unit
7 Millbank
London SW1P 3JA

20 November 2014

Dear Mr Hook

Taxation of Pensions Bill 2014

1. The Institute and Faculty of Actuaries (IFoA) welcomes the opportunity to respond to this consultation. The response has been prepared by some of our members who advise sponsors and trustees of pension schemes with support from members of our Pensions and Long Term Care Working Party.

2. The IFoA is the chartered professional body for actuaries in the United Kingdom. Actuaries' training is business focussed, founded on quantitative risk analysis techniques and is applied across a broad range of fields. Most commonly actuaries work for insurance companies or pension funds, either as a direct employee or in firms that undertake work on a consultancy basis. Members of the profession have a statutory role in the supervision of pension funds and insurance companies.

3. We have focused our evidence on those areas where our members have relevant experience and expertise.

4. Given the far reaching nature of the reforms to the pensions framework, the IFoA would encourage policymakers to consider the interaction between this Bill and other forthcoming legislation - in particular, the requirement for guidance in the Pensions Scheme Bill (paragraphs 4 to 6) and the changes to providing for social care costs (paragraph 7). We would suggest that, across both these areas, greater clarity is necessary in advance of April 2015, to ensure that pension scheme members understand the financial consequences of the various legislative changes on their choices and decisions at, and during, retirement.

5. The flexibility introduced into the pensions regulatory environment by the Budget has created a more complex taxation environment for many pension scheme members. The Chancellor has confirmed that pension scheme members will have access to a guidance service, which will include information about their benefits at the point of retirement. A key question is whether this will be comprehensive enough. It is clear that the additional complexity arising from taxation considerations is, in some circumstances, going to require further information than would be available in a short guidance session.

6. If the implementation of the new retirement income flexibilities is to be successful for as many retiring scheme members as possible, the guidance provided will need to highlight the potential tax implications for certain types of decision. The objective being to overcome the risk that retiring pension scheme members face unexpected tax payments.

7. If the initial guidance cannot cover the complexity of an individual's tax circumstances, the IFoA suggests the Pension Scheme Bill, currently passing through Parliament, leads to regulations that ensure members are signposted to take further advice, in order that they can take decisions that are appropriate for their circumstances.

8. The IFoA believes it is important for individuals to be able to understand the interaction of the pensions tax regime and the financial assessment for social care costs in later life. While this goes beyond the specific content of the Bill, we would encourage HM Treasury and the Department of Health to indicate clearly how pension funds, within different decumulation vehicles, would be treated. For example;
    a. If uncrystallised funds and drawdown pots are treated as assets, many pension scheme members may be unaware that they could face significant care costs in later life.
    b. Where an individual elects to take their retirement income through an annuity, with an enhancement for long term care needs, the benefit is currently taxed as 'earned income'. This could have a significant tax impact, particularly where it takes someone into a higher rate band.
    c. If an individual opts to withdraw a lump sum for a specific purpose (such as to pay off debts or to contribute to an offspring's house deposit) and they are temporarily in possession of their withdrawn pot at the time of a social care assessment, this could affect their eligibility for means-tested support.
    d. Where an individual opts to withdraw a lump sum, it is not clear how the withdrawal of pensions for a specific purpose will impact the 'deprivation of assets' rule in the care assessment, if that purpose is not deemed to be essential.

    This interaction is complex, but is important for individuals to consider when making financial plans about their income during retirement.

9. With regard to the specific content of the Bill, we have focused our comments on the transfer on death of an uncrystallised, or drawdown, pot to a beneficiary which leads to a separate consideration of those funds for the Lifetime Allowance (LTA). It is possible that an individual could be the beneficiary from more than one source. The Bill suggests that the separate treatment of these funds could potentially allow an individual to accumulate assets that significantly exceed the LTA. Indeed, an individual could accumulate up to the LTA for each separate transferred fund held. Theoretically, such transfers could take place across a number of generations with no restriction on tax-free investment growth.

10. The IFoA would welcome clarification that this is the policy intent. If that is not the case, there are alternative approaches in dealing with inherited funds. These could include the aggregation of all pots for comparison against the LTA, or a limit on the number of transfers for a pot arising from one source. These alternative approaches could have unintended consequences for dependants and we would welcome the opportunity to discuss this further with the Public Bill Committee.

11. If you wish to discuss any of the points raised please contact Philip Doggart, Policy Manager (philip.doggart@actuaries.org.uk/ 01312401319) in the first instance.

Yours sincerely

Fiona J Morrison
President-elect, Institute and Faculty of Actuaries