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Tax, its that simple

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The emergency budget introduced several interim measures with further consultation planned.

On the changes to the tax treatment of death benefits and the requirement to take benefits at age 75 a new approach is needed.

The Government has proposed many changes:

- No formal requirement to take benefits from a pension scheme at any age, although any benefits remaining uncrystallised after age 75 will be subject to tax charges.
- Alternatively Secured Pension (ASP) will be abolished and individuals currently in ASP will fall into the new regime, but only from 6 April 2011.
- Unsecured Pension (USP) will be split into capped drawdown and flexible drawdown.
 - “Capped drawdown” will be broadly similar to the current USP as we know it but it will not necessarily have the same maximum income limit.
 - Under “flexible drawdown” individuals will be able to draw unlimited amounts from their pension scheme subject to being able to satisfy a Minimum Income Requirement (MIR). Lump sums taken under flexible drawdown will be taxable at the individual’s marginal rate of income tax.
- A uniform tax charge of 55% will be applied to lump sum death benefits paid from pensions in drawdown, and to benefits that have not been put into drawdown where an individual is over the age of 75. This will replace the 35% tax charge currently applied to USP lump sum death benefits, and the (up to) 82% tax charge applied to residual ASP funds.

It is the uniform tax charge that is attracting most of the headlines.

A J Bell has argued long and hard that the existing ASP tax rules represent cliff edge tax policy that is simply unfair. With no tax on death on pre crystallised funds and a 55% charge on crystallised funds a cliff edge remains.

If fairness is a key driver for change why not introduce a simple charge to tax on all residual pension funds irrespective of the age and vested status of the client of say 20% – 25%?

Alternatively, establish a new Compulsory Crystallisation Age (CCA). This will be the back-stop for crystallising benefits and could be anything from 75 to 80. The tax charged on lump sum death benefits could then be:

- 0% from uncrystallised funds,
- 35% from crystallised funds before the CCA,
- 55% from crystallised funds after the CCA.

The current inheritance tax treatment of lump sum death benefits paid in USP should apply irrespective of whether the member is younger or older than the CCA.

These changes can be implemented without pain to the treasury and there is little doubt that they would be fairer for clients and easier to understand.

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Please note this document is intended for trade and national press individuals.

Notes for Editors

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