FROM THE DAY YOU START WORK

YOUR PENSION MATTERS

State and workplace pensions are changing and this will affect you. It is never too soon and rarely too late to start putting extra money aside for retirement, and the taxman will chip in too.

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THINK AHEAD ON PENSION PLANS

With more urgent financial pressures to deal with in our twenties and thirties, many of us give little thought to retirement planning until we hit middle age. The introduction of workplace pension auto enrolment has helped improve awareness and can enable you to start contributing to a pension early in your working life, so that you have time – with the benefit of tax relief on your contributions – to build up a worthwhile pension 'pot' with decades of potential growth, depending how your pension investments perform over the decades.

MIND THE PENSION GAP

Successive governments have taken steps to shift more of the pension-funding burden away from the state; a previous administration brought us stakeholder schemes to make private pensions more accessible and initiated auto enrolment, now being brought in over several years. Linked to this shift were the decisions to let more of us work longer and to make us wait longer for our State Pension; many men and women now at work will have to wait until they are 66, 67 or older to get theirs.

One thing is certain: you cannot be sure how much pension income will await you in retirement or what your income needs will be. You may see a gap of several years between stopping work and starting to collect your State Pension. Your auto enrolment pension may be too little, or too late, to make a big difference. Now there are the implications of the April 2015 pension changes to consider. So, whether you are 30, 40 or 55, you may need to review the progress of your current plans and weigh them up against your estimated needs in retirement.

THE PENSIONS WORLD IS CHANGING

The State Pension has undergone a major overhaul after failing its MOT.

THE STATE PENSION AGE IS CHANGING

For years, everyone was clear about what their state pension age (SPA) was. Men retired when they reached 65, women at 60. Then, as the government investigated life expectancy projections, they calculated the burden on the Exchequer and saw that they needed to gradually increase the state retirement age. By 2020, both men and women's SPA will be 66, increasing to 67 between 2026 and 2028. It will then be reviewed every five years and linked to life expectancy. The increase in age is gradual, and you can find your SPA by using the government's online calculator at Gov.UK.

If you reached state pension age on or after 6 April 2016, you will receive the new flat-rate or 'single tier' state pension of £155.65 per week. One area of confusion surrounds who will receive this new amount. It's important to be aware that the new flat-rate pension doesn't apply to those already in receipt of their state pension. However, there is some good news for this group. The basic state pension increased by 2.9% to £119.30 per week from April 2016. This rise will be worth an extra £174.20 a year to someone currently in receipt of the full state pension.

QUALIFYING YEARS

In order to receive the full amount of the new flat-rate pension, you need 35 'qualifying years' of National Insurance contributions or National Insurance credits. If you have missing years in your contribution record, then you won't qualify for the full state pension when you retire. You can top up your National Insurance contributions to improve the amount you will receive. If you want to get an estimate of what your entitlement would be, you can do so by going to the Gov.UK website.

FACTORS AFFECTING YOUR ENTITLEMENT

Most people reaching SPA in the first couple of decades of the new State Pension, may have been 'contracted-out' of the additional State Pension (SERPS, the state earnings related pension scheme or S2P, state second pension) at some point. When people were contracted-out they either paid National Insurance contributions at a lower rate, or some of the National Insurance contributions they paid were used to contribute to a private pension instead of their additional state pension. They may have been contracted out through an occupational pension scheme where their pension was linked to their salary or through an occupational or personal pension scheme where contributions were invested and the final pension was determined by the outcome of those investments, referred to as a defined contribution scheme.

AUTO PENSION MAY NOT SUFFICE

To tackle the inadequacy of the State Pension and shift more responsibility onto employers, the Government is rolling out its auto enrolment scheme. This goes further than the stakeholder pensions introduced earlier, by forcing employers to auto enrol virtually all employees and make a contribution to their pensions, though an employee may opt out and forgo the tax relief and employer contribution. The required minimum payments are limited and may not produce sufficient pension income for your needs.

The changes being made by Government have come at a time when workplace final salary pension schemes have been in decline because many became unviable. This has meant that fewer people than ever can feel absolutely sure of a comfortable retirement unless they get a proper grip on their pension planning. If you feel uncertain about your pension outlook in the shifting sands of the early 21st century, including the April 2015 changes, a full review with the benefit of expert advice is recommended.

THE TAXMAN HELPS TOO

Putting money aside for the long-term future can be a challenge when there are things like mortgage payments and the cost of raising a family to think about, but the financial impact can be softened by the benefit of tax relief. For every £100 that a standard rate taxpayer puts into a pension, the taxman adds £20 in the form of income tax relief, giving your hard-earned cash a head start in the quest to achieve long-term growth. As a higher rate taxpayer you could save even more tax.

The tax incentive to invest for retirement has been around for many years, but it is not unlimited. There are both annual and lifetime allowances that restrict how much you can put in and qualify for tax relief. These limits have been reducing and, currently stand at £40,000 and £1 million, respectively. From 2016-17, the annual allowance tapers from £40,000 to £10,000 if income exceeds £150,000. From 6 April 2016, an individual with a taxable income (excluding pension contributions) of £110,000 or more could see their annual allowance decrease from £40,000. The taper has been introduced so that these higher earners will have their annual allowance reduced by £1 for each £2 by which their 'adjusted income' exceeds £150,000; subject to a minimum annual allowance of £10,000 for individuals with an adjusted income of £210,000 or more.

Whatever stage of your working life you may be at currently, this changing world of pensions dictates that you should put the more immediate day-to-day demands to one side for a moment and contemplate an old age fraught with financial pressures

BENEFITING YOUNG AND OLD

The tax relief available on pension contributions may apply to payments you make on behalf of other people, perhaps your children or grandchildren, even if they have no earnings. In these circumstances, contributions eligible for tax relief are limited to £3,600 per annum gross (£2,880 net with standard rate income tax relief). This can be a useful tax-efficient method of long-term saving, provided that tying the money up until the beneficiary is 55 or older suits your intentions.

The taxman's largesse goes even further, to the time when a pension becomes payable. HMRC rules usually allow people taking their defined contribution pension to draw up to 25% of their 'pot' tax-free, whether as a one-off lump sum or with the option of spreading it over time. You may find this a useful source of money for investment, future planned spending or emergencies. The decision and the tax-free sum calculation may not always be simple, in which case advice from a pensions professional can help.

FUTURE INCOME IN YOUR HANDS

More of us have to think about our future pensions than was the case in the past. More people had copper-bottomed final salary pensions 20 or 30 years ago, but financial crises and rising life expectancy left many schemes under-funded and caused them to close to new members or go cap-in-hand to the Pension Protection Fund. Most schemes now operate on a defined contributions (money purchase) basis that depends directly on investment performance.

The trend towards money purchase schemes, coupled with changes to the State Pension and when it is payable, has made it more difficult to know whether your state and other pensions will really be enough to see you comfortably through what could be a very long retirement. The new flat rate State Pension, plus several years or more of auto enrolment in a workplace scheme may just about cover the essentials of later life, but not necessarily the extra comforts.

GETTING PERSONAL

Whatever stage of your working life you may be at currently, this changing world of pensions dictates that you should put the more immediate day-to-day demands to one side for a moment and contemplate an old age fraught with financial pressures. There are ways to supplement your expected pension income, from AVCs (additional voluntary contributions) to personal pensions, that enable you to increase your level of tax-relieved saving towards a higher pension income.

With your contributions enhanced by the addition of tax relief, long-term investment in assets with growth potential through a personal pension, or a group personal pension provided by your employer (some are being set up for auto enrolment), could make a big difference to your retirement. Some high earners, business owners and directors may, however, prefer less restrictive alternatives that allow their pension savings to provide for their retirement and aid their business in the meantime.

THE SELF-MANAGED ALTERNATIVES

The virtual demise of final salary pensions and the redundancies in middle management, which have led to the creation of many new businesses, have left some of the more entrepreneurial pension investors looking for alternative ways to secure their retirement. Many of them have found an answer in the Self-Invested Personal Pension (SIPP) and Small Self-Administered Scheme (SSAS), which offer the freedom and flexibility to help them achieve personal and business objectives.

Investments permitted within a SIPP normally include quoted and unquoted shares, collective investments, gilt-edged stock, overseas equities, cash deposits, insurance bonds and commercial property. A SIPP may also borrow an amount up to half of its net assets, subject to HMRC rules. In some circumstances, your SIPP may be a suitable vehicle for owning your business premises.

SASSY BY NATURE

A SSAS can also make investment choices from a wider range of options than a normal pension, involving added opportunities but also risks that you need to think about. The scheme can be tailored on a one member or multi-member basis. It can invest in much the same range of assets as a SIPP and can similarly borrow within limits, whether from a commercial lender or a connected person on commercial terms. Employer contributions can usually offset corporation tax.

The added freedom of choice and possibility of higher returns that go with some asset classes and the use of borrowed funds make professional advice essential when contemplating a SIPP or SSAS; some assets, for instance, involve a greater degree of price volatility or risk of loss. That said, the flexibility continues, as you can crystallise pension benefits any time from age 55, using annuity purchase or the pension drawdown option now more readily available under the 2015 pension freedoms.

NOW MORE CHOICES WHEN YOU RETIRE

After years of making tax-efficient contributions, the time to think about reaping the benefits can suddenly come into view. As retirement approaches, you will need to start looking at how best to use your pension fund to generate income when you need it and the April 2015 changes open up wider options for more people. You may still use your pension pot to buy an income for life, an 'annuity', but many people are opting for the new freedom to draw what they want, when they want, from their pension pot and perhaps to leave a large part reinvested for future income and potential capital growth to fund later retirement needs.

The flexibility and freedoms opened up in April 2015 are enormous and, for some, mean facing quite daunting decisions. These are the main features of the new pension regime for defined contribution schemes, subject to the terms of your specific scheme:

- Flexible access to pensions from age 55
- The 25% tax-free entitlement may be spread over time
- Final salary pensions can be switched to defined contribution pensions; however some transfers from public sector schemes will no longer be allowed
- Retirement age set to increase from 55 to 57 from 2028 (thereafter 10 years below State Pension age)
- Death benefits paid to beneficiaries on death before age 75 are paid tax free if designated within 2 years
- Death benefits paid on death after 75 are subject to the beneficiary's marginal income tax rate if not designated within 2 years and will be taxed if taken as a lump sum; if you live beyond your 75th birthday, or if you die earlier but your pension funds are not designated within 2 years, the death benefits will be taxed

If you envisage buying an annuity, a few years before your retirement is due, you should review your investment risks and take advice on whether your pot should be held in a lower-risk fund for the two or three years before you expect to buy your annuity, to protect the value. A single life annuity pays you a set amount of income for the rest of your life; a joint life annuity will continue to pay a surviving spouse or partner at a specified rate.

The so-called 'open market option' enables you, ideally with your adviser's help, to shop around for an annuity that provides best terms for your needs, depending on your health and whether you choose a level or a rising income.

With a drawdown pension, the income received may be varied but is not guaranteed for your lifetime, but you can keep some (perhaps a large part) of your pot invested. Whether you plan to choose drawdown or an annuity, or even a combination, make sure you get professional advice before making a decision, as the 'guidance' offered on behalf of the Government is limited in its scope.

TAKE CONTROL OF YOUR PENSION OUTLOOK NOW

It is important to take professional advice before making any decision relating to your personal finances. Information within this document is based on our current understanding and can be subject to change without notice and the accuracy and completeness of the information cannot be guaranteed. It does not provide individual tailored investment advice and is for guidance only. Some rules may vary in different parts of the UK. We cannot assume legal liability for any errors or omissions it might contain. Levels and bases of, and reliefs from, taxation are those currently applying or proposed and are subject to change; their value depends on the individual circumstances of the investor. No part of this document may be reproduced in any manner without prior permission.

The value of investments can go down as well as up and you may not get back the full amount you invested. The past is not a guide to future performance and past performance may not necessarily be repeated. If you withdraw from an investment in the early years, you may not get back the full amount you invested. Changes in the rates of exchange may have an adverse effect on the value or price of an investment in sterling terms if it is denominated in a foreign currency.

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