Taxation of Pensions Bill 2014-15 – debates in Parliament

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At present, most people with defined contribution (DC) pension savings use them to buy an annuity. This is because pension tax legislation allows lump sum or flexible withdrawals only in limited circumstances. In Budget 2014, the Government announced that from 6 April 2015, people aged 55 and over would be able to access their DC pension savings when and how they choose, subject to their marginal rate of income tax.

The *Taxation of Pensions Bill* would make changes to pension tax legislation to implement this. It would also restrict and reduce certain tax charges applying to death benefits. The Bill was published on 14 October 2014 and had its Second Reading in the House of Commons on 29 October. This was followed by four sittings of a Public Bill Committee between 11 and 20 November. During Committee stage, the Government made twelve amendments to the Bill and added a new clause to introduce a new schedule – regarding the tax treatment of unused funds on the death of a pension scheme member. Each was accepted without division. Two Opposition amendments were negatived on division. The Bill had its Report Stage and Third Reading on Wednesday 3 December 2014. The Government amended the Bill to simplify the reporting requirements on individuals who have flexibly accessed their savings. One Opposition amendment was defeated on division. The Bill had its First Reading in the House of Lords, when it was endorsed as a Money Bill. It had its Second Reading and remaining stages in the Lords on 16 December 2014. The *Taxation of Pensions Act 2014* received Royal Assent on 17 December 2014.

This note is a guide to debates in Parliament. The provisions in the Bill are discussed in more detail in Library Note SN 6891 Flexibility for DC pension savers from April 2015 (December 2014). The changes to pensions legislation necessary to implement the Budget announcement (for example, provision for a guidance guarantee and relating to transfers from defined benefit schemes) are in a separate Bill - the *Pension Schemes Bill 2014/15.* For more detail, see Library papers – RP 14/44 *Pension Schemes Bill* and for the debates in Parliament SN 7030 and SN 7105.

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1 Background

At present, most individuals with defined contribution (DC) pensions use them to purchase an annuity. This result is strongly encourage by current pension tax legislation, which allows lump sum or flexible withdrawals only in specified circumstances.

In Budget 2014, the Government announced that from April 2015, individuals aged 55 and over would be able to choose when and how to access their DC pension savings, which would be subject to their marginal rate of income tax. This Bill sets out the changes to pensions tax legislation needed to implement this. Under its provisions, the main options available to people from 6 April 2015 would be to:

- Purchase a lifetime annuity that would provide an income throughout retirement (with some current restrictions removed);
- Designate funds to a 'flexi-access drawdown fund', with no restrictions on the amount of withdrawals that can be made; and
- Take an 'uncrystallised funds pension lump sum' (UFPLS), which means individuals would be able to make withdrawals from money purchase pension savings that haven't yet come into payment, without first creating a flexi-access drawdown fund.

People already in a 'capped' drawdown on 6 April 2015 could convert to flexi-access drawdown. Existing flexible drawdown funds would become flexi-access drawdown funds.

In the case of a lifetime annuity or flexi-access drawdown, there would normally be the option of a 25% tax-free lump sum at the time of taking the pension. For UFPLS, 25% of each

withdrawal would be tax free. Where an individual has accessed their DC pension savings 'flexibly', the amount they can contribute annually to a money purchase scheme would reduce to £10,000.

Other changes in the Bill would restrict and reduce certain tax charges applying to death benefits and reduce the age limit for taking small amounts of savings as a lump sum from 60 to 55, or earlier in cases of ill-health.

The background to the changes is in the RP 14/57 Taxation of Pensions Bill (23 October 2014).

This Bill makes the changes to tax legislation necessary to implement these reforms. The necessary changes to pensions legislation are in the *Pension Schemes Bill 2014/15*. As presented to Parliament, the Bill included provision for a prohibition on transfers from unfunded defined benefit public service schemes, except to other DB schemes. A number of amendments were made at Committee Stage and Report Stage included provision for a guidance guarantee. The background to the Bill is in RP 14/44 Pension Schemes Bill (August 2014). For a guide to debates in Parliament, see SN 7030 Pension Schemes Bill 2014-15 – House of Commons stages (November 2014).

2 Second Reading

The *Taxation of Pensions Bill 2014-15* [Bill 97] was published on 14 October 2014 and had its Second Reading on 29 October 2014.

Financial Secretary to the Treasury David Gauke MP explained that the first main change in the Bill was to make unlimited drawdown available to people with defined contribution pension savings from April 2015:

> At Budget 2014, the Chancellor announced that everyone with a defined contribution pension could take it as they wished from age 55, and would no longer be subject to drawdown limits or income tests before being able to take their money flexibly. The current system denies people flexibility at the point of taking their pension. For those with the smallest and largest pension savings, there is the option to take their pension as cash, but for everyone else there are considerable restrictions. They have two main options: purchase an annuity or enter capped drawdown. Capped drawdown limits how much someone can take out each year to an amount calculated by reference to the amount they might have received from an annuity purchased with their fund.
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> Flexible drawdown already lets those with very high levels of savings to take their money however they want, taxed at their marginal rate, if they can prove that they have a guaranteed pension income for the rest of their life of at least £12,000. The Government have already reduced that from £20,000 to give many more people flexibility, but the first main change provided for in the Bill goes much further, making unlimited drawdown available to anyone with a defined-contribution pension and removing the limits on what can be withdrawn from those funds.
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> The Bill also ensures that existing drawdown funds can, if the individual wants, be converted to flexi-access drawdown, so that those currently in capped drawdown will be able to benefit too. The aim of the changes is to give all the 320,000 people who retire every year with defined contribution savings greater choice about how to access

> those savings, regardless of how big their pension pot is. The changes will take effect from 6 April 2015.[1]

The second main change was to make annuities more flexible:

> Current tax legislation caters for two broad categories of retirement income: lifetime annuities and drawdown. As I have set out, we are making drawdown much more flexible. Let me explain how we are doing the same for annuities.
>
> We think annuities will still be the right product for many people, as they provide the valuable security of a guaranteed income for life. The current requirements for a lifetime annuity, however, lead to an inflexible and restrictive product, and there is a clear demand for more flexible ways of getting income from one's pension pot. We want these reforms to stimulate competition and innovation in the retirement income market. We want providers to innovate and create new products that will more closely reflect the changing needs of their customers. We have consulted extensively with industry on the changes that it would like us to make to enable this kind of innovation. The Bill will deliver those changes by allowing annuities to decrease, and by removing the 10-year guarantee period for guaranteed annuities. That gives significantly more flexibility to providers to offer products that meet individuals' needs more closely. Those changes will apply to annuities sold after 6 April 2015.[2]

The third main change was to introduce a new method by which people can access their pension – an uncrystallised funds pension lump sum - with 25% of each payment tax-free:

> Currently, people who want to take their pension as cash have to take their whole tax-free lump sum—25% of their fund—and place the other 75% in a drawdown fund. Any money they then draw down is taxed at their marginal rate. The Bill will introduce a new option by giving individuals the flexibility to take one or more lump sums from their pension fund—with 25% of each payment tax-free and 75% taxed at their marginal rate—without having to enter into drawdown. This lump sum is known as an uncrystallised funds pension lump sum, or an UFPLS. *[Interruption.]* It is perhaps not the most elegant of names, but try doing better with "uncrystallised funds pension lump sum". These payments can be taken from funds that are uncrystallised—that is, have not yet been accessed. It will be open to schemes to provide this option from 6 April 2015 onwards. This does not change the amount of tax people pay on their pension, but it does provide them with extra flexibility and further choice about when and how to access their savings in a way that suits them.[3]

He said the Bill included measures intended to ensure the reforms are not exploited for tax purposes:

> If the Government were to take no action, an individual over the age of 55 could divert their salary each year into their pension, take it out immediately and receive 25% of it tax-free, thus avoiding income tax and national insurance contributions on their employment income. That is not the intention of the reforms.
>
> The Government spend a considerable amount a year on pensions tax relief and have a responsibility to ensure that the money is used for genuine pension saving. Under the current system, individuals in flexible drawdown have no annual allowance. They are not entitled to tax relief on anything that they contribute to their pension after they have accessed it flexibly. Extending this rule under the new system would be

[1] HC Deb 29 October 2014 c323

[2] Ibid c327

[3] Ibid c327

> disproportionate and would disadvantage average savers. We are in an era of much more flexible retirement. An individual might access their pension flexibly and then decide to return to work, or access it while working. They might still want to save into a pension. They might be automatically enrolled into a pension and be subject to a tax charge on the amount contributed. If we kept the current system, there would be a strong incentive to opt out of auto-enrolment.
>
> Instead of having no annual allowance, individuals who access their pensions flexibly will, under the new system, have a lower annual allowance of £10,000, which will apply to their defined contribution savings. This approach allows people the flexibility to contribute to their pension even when they have flexibly accessed their pension rights. At the same time, it ensures that individuals do not use the new flexibilities to avoid paying tax on their current earnings. It will prevent those with the means to divert large sums into pensions from doing so, while allowing the vast majority of individuals to continue to save. The Government have worked very closely with industry to develop this measure, and will continue to do so to ensure that it remains fair and proportionate.[4]

Other measures in the Bill included

> […] the introduction of a permissive statutory override, which will allow schemes to make the types of payments set out in this Bill without the need to change their scheme rules; provisions to ensure that the new system is reflected in the rules governing overseas schemes involving UK tax-relieved funds; allowing payments from guaranteed annuities to be paid to beneficiaries as a lump sum if they are under £30,000; and measures to ensure that people cannot gain an unintended tax advantage by becoming temporarily non-resident.[5]

Further information on the estimated Exchequer impact of the reforms, including the impact of the measures announced since the Budget, would be made available at the time of the Autumn Statement. These estimates would be certified by the Office for Budget Responsibility.[6]

Shadow Financial Secretary to the Treasury Cathy Jamieson said the Opposition supported "increased flexibility and choice for savers" which was why it had "long advocated reform of the annuities market to help people shop around to get a better deal."[7] However, it had concerns, in particular regarding the speed with which the reforms were being introduced.[8] It had set out three tests against which it thought the reforms should be measured:

> The first was the advice test: would there be robust advice for people on providing for their retirement and measures to prevent mis-selling? The second was the fairness test: that the new system would be fair, with those on middle and low incomes still being able to access the products that give them the certainty in retirement that they want. The third was the cost test: that the Government must ensure that these reforms do not result in extra costs to the state, either through social care or pensioners falling back at a later stage on means-tested benefits such as housing benefit. We stand by

[4] Ibid c327-8
[5] Ibid c329
[6] Ibid c329
[7] Ibid c330
[8] Ibid c330

> those tests and would argue that so far, the Government have been unable to give assurances on any of those points.[9]

Regarding the guidance guarantee, to be introduced under the *Pension Schemes Bill 2014-15,* she said:

> That guarantee is integral to the measures in the Bill, because if the Bill is to be a success, the guidance must be fit for purpose. It is not unfair to say that the continuing concerns and confusion over the guidance guarantee do not give confidence to people who are worried about how they are going to access the guidance.[…] The crux of the matter, and what the consumer needs to understand, is: what will the guidance consist of? Will it be an interactive exchange, or will it be a list of questions that must be asked and areas that must be covered?[10]

Responding to the debate, Exchequer Secretary to the Treasury, Priti Patel explained how the guidance guarantee was developing:

> The aim of guidance is to empower consumers to make informed and confident decisions on how to use their pension savings in retirement. Information alone is not enough to change consumer behaviour. The Government are committed to maximising awareness of the guidance service. Key to that will be the regulatory requirements on providers and schemes to signpost to guidance at key points when individuals are trying to access their pension pot. In its recent consultation on the changes surrounding new pension flexibilities, the FCA has been clear about requiring genuine signposting, including rules that ensure firms cannot circumvent consumers' right to guidance. An essential part of the development of the guidance will be determining what engages consumers effectively. The Government are assessing engagement and take-up rates, and testing different engagement strategies informed by behavioural insight teams as part of piloting work beginning this autumn. […] The scope of the high-level content of the guidance was set out in the FCA consultation that it ran in anticipation of its standard-setting role. The Treasury and its delivery partners, the Pensions Advisory Service and Citizens Advice, are working up the operational details and the context of the guidance while adhering to the FCA standards.[11]

The Bill was given a Second Reading without a vote.[12]

3 Public Bill Committee

The Public Bill Committee was chaired by Mike Weir and Nadine Dorries. As well as Financial Secretary to the Treasury, David Gauke, and Shadow Financial Secretary, Cathy Jamieson, its members were:

Barwell, Gavin *(Lord Commissioner of Her Majesty's Treasury)*
Bridgen, Andrew *(North West Leicestershire)* (Con)
Dakin, Nic *(Scunthorpe)* (Lab)
Djanogly, Mr Jonathan *(Huntingdon)* (Con)
Evans, Chris *(Islwyn)* (Lab/Co-op)
Freer, Mike *(Finchley and Golders Green)* (Con)
Glass, Pat *(North West Durham)* (Lab)
James, Margot *(Stourbridge)* (Con)

[9] Ibid c332
[10] Ibid c336
[11] Ibidc359-60
[12] Ibid c362

Mills, Nigel *(Amber Valley)* (Con)
Nash, Pamela *(Airdrie and Shotts)* (Lab)
Opperman, Guy *(Hexham)* (Con)
Pearce, Teresa *(Erith and Thamesmead)* (Lab)
Robinson, Mr Geoffrey *(Coventry North West)* (Lab)
Shannon, Jim *(Strangford)* (DUP)
Smith, Henry *(Crawley)* (Con)
Stephenson, Andrew *(Pendle)* (Con)
Swales, Ian *(Redcar)* (LD)

The Committee sat four times. At its first sitting on the morning of 11 November 2014, it took oral evidence from witnesses from a range of organisations: the Financial Conduct Authority; the Financial Services Consumer Panel; Citizens Advice; Scottish Widows; Legal and General; Association of British Insurers and HM Treasury.

Written evidence was received from: Partnership TP18; National Association of Pension Funds (TP14); National Association of Pension Funds - supplementary (TP15); Financial Conduct Authority (TP16); Britannia Financial Services Ltd, Auckland, New Zealand (TP17); Mark Hattersley TP05; Towers Watson (TP06); Just Retirement (TP07); Friends Life TP08; Talbot and Muir (TP09); John Greenwood (TP10); Hargreaves Lansdown (TP11); Association of Taxation Technicians (TP12); ABI (TP13); Low Incomes Tax Reform Group (TP01); Association of Consulting Actuaries (TP02); Ros Altmann (TP03); Stephen Ward (TP04).

The provisions of the Bill were then considered over three sittings:

Second sitting – 18 November 2014 (morning)
Third sitting – 18 November 2014 (afternoon)
Fourth sitting – 20 November 2014 (morning)

The Government made twelve amendments to the Bill and added a new clause to introduce a new schedule – regarding the tax treatment of unused funds on the death of a pension scheme member. Each was accepted without division. Two Opposition amendments were negatived on division. One would have required the Treasury, within six months of Royal Assent, to publish any analysis it had prepared by it prior to the publication of the Bill. The other would have required a review of the impact of the Act within one year of Royal Assent.

4 Debate on the clauses

As presented to Parliament, the Bill [Bill 97] had three clauses and a Schedule:

- Clause 1 introduced the Schedule, which contains most of the detail;
- Clause 2 restricted and reduced the tax charges that apply to certain lump sums;
- Clause 3 contained definitions that apply to this Bill and a power to amend specified legislation in consequence of this Bill.

4.1 Clause 1 – provision for pension flexibility

Introducing clause 1, Financial Secretary David Gauke explained:

> The changes in the Bill will address that by increasing flexibility for those retiring with a defined contribution pension. They will allow people more choice about how they use their pension savings to fund their retirement. The schedule introduced by clause 1 makes changes to create flexi-access drawdown, which has no caps or income requirements. It makes annuities more flexible, creates a new way to take money directly from a pension, prevents those reforms from being exploited for unintended tax purposes, and ensures that the new UK pension system is reflected in the treatment of relevant overseas schemes.[13]

Shadow Financial Secretary Cathy Jamieson said that the success of the reforms would be judged on the outcomes:

> We all want better outcomes. We have always been clear in our support for those principles of greater freedom and choice, but the effectiveness of a Bill can only ever be judged by what it does in practice and what the outcomes are. [14]

It would be important to ensure savers got the "right guidance". A particular concern related to the way the reforms had been communicated:

> One concern expressed by both the industry and those who will be giving guidance under the guarantee is that the intention behind this Bill, and perhaps the Pension Schemes Bill as well, has been caught up in the spin and hype about people being able to access massive pension pots to buy a Lamborghini, take a holiday and pay off the mortgage, while the same emphasis has not been put on the fact that the purpose of a pension is to provide for people's lifetime in retirement. We have heard that people often do not think about the length of time over which their pension will have to provide for them, or about the standard of living that they want to have during that period.[15]

She asked about the impact of the reforms on the claims for means-tested benefits:

> As I was saying, the notional income rules apply to people who have reached the qualifying age for pension credit, currently linked to the state pension age for women, which started to rise from 60 in April 2010 and will reach 65 in November 2018. The rules do not apply to people of working age. They allow a person to be treated as having taken income available to them under a personal pension plan, even though they have not applied for it. Those rules are outlined in the State Pension Credit Regulations 2002—S.I. 2002 No. 1792, if anyone wants to look at the detail. Given that someone with flexible drawdown is unlikely to qualify for pension credit, it might be argued that that is not an issue, but it appears that it may mean that a person with an occupational pension is treated as having the amount they could withdraw under capped drawdown, even if they have not accessed that income.
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> Following the changes announced in the Budget and included in the Finance Act 2014, the maximum amount that can be drawn down under capped drawdown is now 150% of an equivalent annual annuity, so it is fair to assume—unless the Government tell us otherwise, and I am sure the Minister will want to comment—that this may be the benchmark amount for measuring an individual's notional income. However, after the reforms in this Bill, many of those who were in capped drawdown will no longer be so and will no longer be covered by the capped drawdown rules, so an alternative

[13] PBC Deb 18 November 2014 c46
[14] Ibid c48
[15] Ibid c49

> benchmark for assessing an individual's notional income may be required. If the Minister is able to clarify, I would welcome it.[16]

She said evidence to the Committee on the issue had been unclear. A representative of Citizens Advice had said the rules on deprivation of assets and notional income might not need to change, but there might need to be additional clarification and communication with consumers.[17] A Treasury Official had said:

> We have said that the principle is that the decision that you make on how you access your pension should not significantly affect how you are judged or measured for social care or welfare. We will make sure that, whatever the product choice you make, you are treated in a consistent way, whether that is in flexi-access or through an annuity, so that the treatment across the board is fair and consistent.[18]

Ms Jamieson thought this evidence indicated a "lack of clarity on the issue."[19]

She thought evidence to the Committee on the costs of social care had raised two issues – how flex-access drawdown would affect entitlement to help with the costs and whether there was an increased risk of people exhausting their savings prematurely. The ABI had expressed concern that:

> […] a continued focus on early access at the age of 55 means that there may be barely enough in the pension pots of some savers to cover their near-term retirement income needs, let alone enough left to stretch to care costs in older age." [20]

She said people would see a contradiction in the emphasis on early access to pensions at the same time as people were being encouraged to think more about their longer term future.[21]

Geoffrey Robinson said there was a danger that people would not realise there were "no clear rules" governing uncrystallised funds pension lump sums. He referred to written evidence from the ABI, which had said that the "regulatory rules affecting a number of key changes in the Bill are not yet clear":

> 13. For instance, the FCA is urgently considering the regulatory position around accessing a pension pot in one lump sum – whether through Flexi-Access Drawdown or an Uncrystallised Funds Pension Lump Sum – but the longer this remains unclear, the more difficult it is for providers to plan and develop requisite systems. This is despite that taking a pension pot in this way was a key expectation raised as a result of the Budget reforms. Similarly, the whole regulatory regime around the Uncrystallised Funds Pension Lump Sum route which forms the basis of the Government's 'pension bank account' analogy has yet to be resolved. In addition, there could be gaps in regulation between contract-based and trust-based schemes in two key areas. Firstly, how drawdown in trust-based schemes will be regulated; secondly, protection for

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[16] Ibid c50-1
[17] PBC Deb 11 November 2014 c26, Q45
[18] Ibid c30 Q51-2
[19] Ibid c52
[20] Ibid c52; Written evidence submitted by ABI (TP 13)
[21] Ibid c53

> customers and expectations of providers, if a customer wants to transfer out of a defined benefit scheme after receiving advice not to do so.[22]

In response, David Gauke said the guidance guarantee was a priority for government:

> It is very much a priority of the Government to ensure that that guidance is of the quality that we need, and all the parties involved are putting in a huge amount of effort to ensure that the guidance is available in time for April and is as effective as possible. The objective of the guidance is to empower consumers to make informed and confident decisions on how they use their pensions savings in retirement, and the standards are designed to ensure maximum consumer engagement with the guidance, to ensure that people are confident of the options open to them and have a hand-off document that is of practical use.[,…] All the delivery partners, including the Treasury, will work out the operational detail while ensuring adherence to the FCA's standards. It is right that the guidance is available in a variety of different forms—online, over the phone, or face to face—and that it is tailored for individuals' personal circumstances. The guidance will have to meet FCA standards, which it has recently consulted on. The FCA has an important role to ensure that the points the hon. Gentleman raised about the guidance being clear, consistent and understandable are met.[23]

The rules regarding the notional income to be assumed to particular pension products were under consideration and would be confirmed in due course:

> Essentially, there is no change to the principle behind the rules. Notional income will be assigned to a drawdown product, so there is no change there.[24]

Regarding the argument put by witnesses including the ABI that there should be a "second line of defence" (i.e. the information that is provided by providers to consumers who may or may not have taken up the offer of guidance) he said:

> The FCA is looking at a requirement that providers give their customers a description of the possible tax implications when they require access to their pension fund. Those who do not take the guidance will receive the information about their options as they currently do, including about being able to shop around on the open market and so on.[25]

In response to arguments that there had been too great an emphasis on early access in communicating the reforms, he said the Government had always been clear that under tax rules individuals may be able to access their savings from age 55. It had also announced its intention to raise the minimum pension age from55 to 57 in 2028. The Government started from the view that if there were restrictions to be placed on access to a pension pot, they should be minimised.[26]

The Committee agreed that clause 1 should form part of the Bill.[27]

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[22] Written evidence submitted by the ABI (TP 13), November 2014
[23] PBC Deb 18 November 2014 c56
[24] Ibid c58
[25] Ibid c58-9
[26] Ibid c60-1
[27] Ibid c61

4.2 The Schedule – pension flexibility etc

David Gauke gave an outline of the provisions in the Schedule. This includes provision for a reduced money purchase annual allowance of £10,000 for people who have accessed their defined contribution pension flexibly. Some commentators, including journalist John Greenwood, had raised concerns that although this reduced the potential for 'tax leakage', it did not remove it altogether.[28] Anticipating a question on this point, Mr Gauke said:

> The Government consulted extensively on how best to ensure that the new system cannot be exploited by individuals to achieve unintended tax advantages. If the Government were to put in place no protections, an individual over the age of 55 could divert their salary each year into their pension, take it out immediately and receive 25% of it tax-free, thus avoiding income tax and national insurance contributions on their employment income. This is not the intention of the reforms. However, in the context of automatic enrolment, it is important that any solution preserves the incentive for those over 55 to save after accessing their pension flexibly.
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> […] As a result of extensive consultation, the Government decided that the £10,000 money purchase annual allowance strikes the right balance. On the one hand, it allows people the flexibility to withdraw or contribute to their pension as they choose from the age of 55. On the other hand, it ensures that individuals do not use the new flexibilities—which are intended to provide people with greater access to their retirement savings—to avoid paying tax on their current earnings. It will also avoid unnecessary complexity for both consumers and pension providers when the new system comes into place in April 2015. As stated in the Government's response to the consultation, we will closely monitor behaviour under the new system, and will work closely with industry to ensure that the system remains fair and proportionate.[29]

Government amendments – treatment of unused funds on death

David Gauke introduced Government amendments, the aim of which was to ensure that individuals who die with funds remaining in their pension pots can pass them on to anyone they choose. The funds could then be paid tax-free if the original pension member died before age 75, or taxed at the beneficiary's marginal rate if a person died having reached age 75. The amendments included provision to allow unused funds in the member's drawdown account to be paid out as a lump sum to a beneficiary who is not a dependant, and to be payable from unused drawdown funds on the death of that beneficiary. A new clause and new schedule would allow allows an individual to inherit unused drawdown funds or uncrystallised funds on the death of a member where those funds were then used to provide a drawdown pension or to pay a lump sum death benefit. The changes would ensure that, when the death of the member or beneficiary occurred before age 75, any payments of income withdrawal to a beneficiary would be made tax-free if they were designated within a two-year period:

> That is a complicated area, so it might be helpful if I set out how the current system works and explain how the amendments change it. Under the current system, the tax treatment of an individual's pension at death varies depending on a number of factors, including the type of pension the individual has, whether it is paid out as a lump sum or as a regular stream of income, and the age at which the individual dies. If an individual dies before the age of 75 with an uncrystallised pension fund, that means they have not yet taken a pension. That fund can be paid out to any beneficiary tax-free as a lump sum up to the lifetime allowance, which is £1.25 million.

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[28] Written evidence submitted by John Greenwood, pensions journalist (TP10)

[29] PBC Deb 18 November 2014 c62-3

Similarly, if an individual who is a member of a defined-benefit scheme dies before the age 75, a lump sum can be paid to any beneficiary tax-free. However, if an individual dies with money in a drawdown fund that is paid out to a beneficiary as a lump sum, a tax charge of 55% currently applies, regardless of the age of the individual when they die. If a pension death benefit is paid out as a stream of income instead of as a lump sum, it will be taxed at the dependant's marginal rate. However, it can be paid out only to a dependant defined as a spouse, a child under the age of 23, or someone who is financially dependent on the deceased.

As set out in the original consultation document, which the Government published alongside the Budget, it is likely that the 55% tax charges that currently apply to pensions on death would apply to more people under the new system. If they were retained, it is likely that they would provide an incentive for individuals to remove their savings from their pension to avoid paying the 55% tax charge.

To deliver those changes, the Government have tabled amendments 1 to 12 to the existing schedule. Those changes are linked to the new clause and new schedule, which I will turn to shortly. Amendments 1 to 3 allow for the new type of death benefit lump sum introduced by the schedule—the flexi-access drawdown fund lump-sum death benefit—which allows unused funds in the member's drawdown account to be paid out as a lump sum to a beneficiary, and to be payable from unused drawdown funds on the death of the beneficiary.

Amendment 4 extends the permissive statutory override in part 5 of the schedule to include drawdown pension payments to non-dependant beneficiaries. That will allow schemes to offer that option to their members, even if it is not currently permitted by their scheme rules. Amendments 5 to 8 amend paragraphs 81 and 82 of the schedule, and ensure that income withdrawals from a non-dependant beneficiary's drawdown fund that was registered under a pension scheme when the beneficiary was temporarily non-resident are treated as accruing when the person returns to the UK.

Amendments 9 to 12 ensure that any payments by a non-UK pension scheme during a temporary period of non-residence that would have been income withdrawals from a drawdown fund if the scheme were a registered pension scheme are treated as arising when the person returns to the UK. These consequential amendments ensure that the legislation contained in the existing schedule is compatible with the Government new clause and new schedule.

The new clause and new schedule make several changes to the current system and will preserve the incentive to save. New clause 1 introduces new schedule 1, which allows an individual—not only a dependant—to inherit unused drawdown funds or uncrystallised funds on the death of a member where those funds are then used to provide a drawdown pension or to pay a lump sum death benefit. The changes ensure that, when the death of the member or beneficiary occurs before age 75, any payments of income withdrawal to a beneficiary will be made tax-free if they are designated within a two-year period. They also ensure that any uncrystallised funds are tested against the deceased's lifetime allowance.

Members may also wish to note that the new clause and new schedule, and amendments 1 and 2, link to clause 2, which reduces the tax charges that apply to certain lump sums paid by pension schemes on an individual's death, and removes the tax charge altogether when an individual dies before age 75. We will be debating clause 2 shortly.

The aim of the changes is to ensure that individuals who die with funds remaining in their pension pots can pass them on to anyone they choose. The funds can then be

> paid tax-free if the original pension member dies before age 75, or taxed at the beneficiary's marginal rate if a person dies having reached age 75. The changes will ensure that individuals who have made sacrifices to save over the course of their lives can pass on their pension savings without worrying about those funds being hit by excessive tax charges when they die. They will also preserve the incentive for individuals to keep money in their pension, without fear of their beneficiaries being hit by a 55% tax charge.[30]

Regarding the treatment of unused funds on death, Cathy Jamieson referred the Government's July 2010 consultation document on removing the requirement to annuitise by age 75, which had stated that:

> On death, pension savings that have been accumulated with tax relief should be taxed at an appropriate rate to recover past relief given, unless they are used to provide a pension for a dependant.[31]

She asked for assurance that the measures in the current Bill would not result in individuals being able to benefit twice from tax relief:

> I wonder how the measures in the schedule fit with that principle. According to the explanatory memorandum, for deaths before the age of 75, lump sum death benefits and flexi-access drawdown pensions from these funds can be paid tax-free, subject, for example, to the member having a sufficient lifetime allowance.
>
> It has been suggested that those two issues do not entirely fit together. We are looking for absolute assurances from the Minister that at no point would anyone be able to benefit twice from tax relief. That is what the principles outlined in July 2010 sought to prevent.[32]

Mr Gauke responded that:

> The primary purpose of pensions is for people's retirement, but if someone dies before they get to use their pension for that purpose, beneficiaries should be able to have those funds. However, we do not want pensions to become a vehicle for inheritance tax planning, so once someone is 75 they will be able to pass the funds on to others in a flexi-access drawdown account, but they will need to pay their marginal rate of tax on them.

The significance of the age of 75 was that it was a "feature of the existing pensions tax system". It was the age at which "individuals stop receiving tax relief on pension contributions, and at which most people will bring their pension into payment."[33]

He clarified the position regarding lump sum death benefits provided in relation to annuities. They would be treated in the same way as other lump-sum death benefits.[34]

The Government's amendments were agreed to.[35]

Reporting requirements

Cathy Jamieson raised concerns about the reporting requirements in Part 6 of the Schedule:

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[30] Ibid c64-5
[31] HM Treasury, Removing the requirement to annuitise by age 75, July 2010, Box 2A
[32] PBC Deb 18 November 2014 c75
[33] Ibid c79
[34] Ibid c79
[35] Ibid c79-81

> […] The guidance to the Bill indicates that those who fail to contact all the providers within a month risk a penalty of up to £300 initially and then up to £60 a day until that information is passed on. Some concerns have been expressed by the pensions industry about the reporting requirements in the Bill.
>
> To be clear about what the legislation sets out, scheme members who flexibly access their pensions after 6 April 2015 will within 31 days receive a statement from the scheme administrator confirming that they have done so. They will then, as I understand it, be required to inform the administrators of all other schemes of which they are a member, as their annual allowance for money purchase arrangements will be reduced to £10,000. That has to be done within 31 days. [36]

She referred to written evidence from Ros Altmann to the effect that:

> This new aspect of the Taxation of Pensions Bill is impractical and will disadvantage many customers. To insist on people notifying all past pension schemes that they have taken some money under flexible access would place an impossible or unreasonable burden on too many people. The fines they would face are also draconian. Many may have only a small sum in an old pension scheme they have lost track of.[37]

Ms Jamieson said the final point was of particular interest:

> […] she appears to believe that the reporting requirements will apply to all pension schemes, whether they are being paid into or not. It is difficult for some to keep track of personal finance and correspondence. We all probably know exactly which pension schemes we are paying into, but people who have moved employment or changed their circumstances may overlook something or find that there is a particular problem.

The Minister said he would listen to concerns on this point and the HMRC would take a pragmatic approach to enforcement:

> Let me first make the general point that we believe that this strikes the right balance. However, we are also prepared to listen to the evidence, the industry and consumer groups. As I outlined to the Committee, HMRC will also take a pragmatic approach to enforcement in this area, which is very important. The focus of the fines is very much on dealing with the deliberate defaulter or the person who seeks a tax advantage in a deliberate way in terms of the maximum penalty of £300. It will be necessary to ensure that individuals are properly informed of the new regime. Schemes need to tell their members when they become subject to the £10,000 allowance. Indeed, that is part of the Bill and the schemes will have a responsibility to ensure that people are aware of that.[38]

The Government has tabled an amendment for Report Stage to simplify the reporting requirements (see section 5 below).

Exchequer impact of the reforms

Cathy Jamieson raised concerns that the Government's expectation of an Exchequer saving from the reforms in the early years was "predicated on the assumption that […] consumer

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[36] PBC Deb 18 November 2014 c70; Written evidence by Talbot and Muir (TP09);
[37] Written evidence submitted by Ros Altmann (TP 03)
[38] PBC Deb 18 November 2014 c76

awareness of the tax implications will be low."[39] Another concern was the potential for tax leakage through salary sacrifice arrangements:

> Increased flexibility may make such options more attractive for those who can afford to receive less of a salary as they approach retirement. It is important to ensure that what the Government intend the tax rules to do actually happens in practice. The Government said that the new rules would
>
> > "ensure that individuals do not use the new flexibilities, which are intended to provide people with greater access to their retirement savings, to avoid tax on their current earnings by diverting their salary into their pension with tax relief, and then immediately withdrawing 25% tax-free."
>
> That is what the Government are trying to do.[40]

The Minister responded that the Government would:

> […] set out details of the policy changes we have announced since the March Budget in the autumn statement, certified by the Office for Budget Responsibility in the normal way.

He said the reforms were "about giving people more choice when they retire, not about raising revenue."[41]

On the potential for 'tax leakage', he disputed the estimates that had been given in evidence and argued that the Government's approach took the right balance. However, it would keep the issue under review:

> We believe that the £10,000 annual allowance sets the right balance but, as I made clear, we would need to review that decision if we found evidence to the contrary. However, we think that that is the appropriate approach to allow the majority of people the flexibility to withdraw or contribute to their pension as they choose, while ensuring that individuals do not use the flexibilities to avoid paying tax on their current earnings.
>
> Under the current system, individuals in flexible drawdown have an annual allowance of zero, but that relates to a relatively small number of people. Under the new system, anyone can enter drawdown, so this approach would be disproportionate and disadvantage savers. It is right that we reform this area. We want to encourage pension saving, particularly in the context of automatic enrolment. We will closely monitor behaviour under the new system. If it becomes clear that the new system is being abused, we will not hesitate to take further action.
>
> HMRC takes a great deal of action to address tax avoidance. On 5 November this year, HMRC issued a list of the 10 things that a tax avoidance scheme promoter will not always tell someone. The list sets out the risks that people face when they sign up to a tax avoidance scheme, including possible monetary costs, reputational damage, and, in some cases, a criminal conviction. We will continue to take action in that area.
>
> The hon. Member for Kilmarnock and Loudoun drew attention to the evidence provided by John Greenwood to the Pension Schemes Bill. He identified significant sums. As the hon. Lady made clear, they are not numbers that we recognise, but some of the assumptions that he used in reaching a very large number required everyone between the age of 55 and state pension age—5 million people—to be employed and taking

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[39] Ibid c72

[40] Ibid c73-4; HM Treasury, Budget 2014, March 2014, HC 1104, chart 1.11

[41] PBC Deb 18 November 2014 c77

advantage of the option to sacrifice salary into a defined contribution scheme. Each individual would reduce their salary significantly and the employer would pay the rest of their salary into their pension.

Each individual would pay an entire year's worth of sacrificed salary into their pension. It would be paid monthly, but they would live off their reduced salary for a whole year before accessing their salary as a lump sum after the end of that year. It was also assumed that the individuals would have enough annual allowance left to do that on top of their employer's current contributions. It is a very unlikely set of assumptions. […] One has to be careful what one means by tax avoidance in this case. We can probably agree that recycling is an artificial, contrived arrangement, as opposed to a situation in which somebody has drawn down flexibly and proceeds to make further contributions. We will keep the matter under review. Our desire is to prevent a significant loss to the Exchequer. We do not want the provisions to be exploited by widely marketed schemes that make use of that particular arrangement, and we believe we have got the balance right. The benefits of engaging in such contrived arrangements are restricted, so the appeal of making use of them in an industrialised, widespread and widely marketed way is severely diminished. I repeat the point that, if we find evidence to the contrary, we would need to come back to the matter.[42]

In response to a question from Ian Swales as to whether annual allowances following flexible access should be limited to those in employment, he said the Government had "no further plans to make restrictions in this area."[43]

4.3 Clause 2 – restriction and reduction of tax charges on certain lump sums

Mr Gauke explained the purpose of clause 2:

Clause 2 amends chapter 5 of part 4 of the Finance Act 2004 to reduce the special lump-sum death benefits charge from 55% to 45%, which applies to certain lump-sum benefits, and also removes the tax charge altogether on such lump sums when an individual dies under the age of 75. It also reduces the serious ill health lump-sum charge from 55% to 45%.[44]

Amendments building on these provisions had already been debated (see section 4.2 above).

Cathy Jamieson asked who would benefit most from this change, saying that the National Association of Pension Funds had said the reality was that it was "likely to affect only those with large pension pots."[45] Mr Gauke responded that "potentially many millions of people would benefit from the threat [of the tax charge] being removed":

I suppose I should also make the point that the well advised were probably always less likely to fall into hitting this particular charge, so probably, all other things being equal, the previous arrangement would have been less likely to affect wealthy individuals having sought advice and so on. The fact is that we have taken this threat away. There was concern that people were inadvertently finding themselves in a position where their estate was being taxed at 55%, whereas if they had acted differently that was less likely to happen. We have removed that threat, as it were.

[42] Ibid c77-8
[43] Ibid c78
[44] Ibid c82
[45] Ibid c82

> Potentially many millions of people will benefit from the threat being removed. That is not to say that millions of people paid this tax charge—they did not—but it does mean that the risk of what could be viewed as a punitive charged is removed. Particularly in the context of more people accessing their pension flexibly, it is right that we made that change, because there was a risk that ever more people would find themselves paying the charge. We have anticipated a problem arising with the system down the line if we do not make the change. That is why we made the changes set out in the clause.[46]

Ms Jamieson welcomed the reduction from 55% to 45% in the serious ill-health lump sum charge.[47]

4.4 Opposition amendment – Pension flexibility: Treasury analysis

Cathy Jamieson moved an amendment to require the Chancellor, within six months of Royal Assent to publish analysis prepared prior to publication of the Bill, including: the distributional impact, a behavioural assessment and the financial risk assessment. The aim was to capture the information which the Government already had:

> We have discussed the principles of the Bill and what it tries to achieve; we now need to drill down into the financial underpinnings, both to understand what is likely to happen and to give us a baseline for the future.[48]

She went on to highlight a couple of issues, such as the impact on the industry. The ABI, for example, had highlighted the need for a sensible and proportionate approach to regulation, saying that:

> Both conduct and prudential regulators will need to take sensible and proportionate approaches to the sale of new products and the capital required behind them, if the Government's ambitions for an innovative market are to be fully met.[49]

The ABI had also raised concerns about the implications for investment in infrastructure, arguing that pension providers would face greater requirements to be 'liquid'.[50]

The financial impact on individuals was also an important issue. The Association of Tax Technicians (ATT) had raised concerns about the impact on the income tax position of pensioners considering taking benefits under the new regime, saying it was:

> […] deeply concerned about the impact on the income tax position of pensioners considering taking benefits under the new regime. A system based on many end-of-year reconciliations being carried out with no legislative framework or structure (such as there is, for example with the self-assessment system where assessments are appealable – P800s are currently not appealable) will only lead to chaos and misery for very many frustrated pensioners.[51]

Ms Jamieson said the tight time-scale for implementation meant that some things had not been fully considered:

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[46] Ibid c83

[47] Ibid c82

[48] Ibid c84-5

[49] Ibid c84; Written evidence submitted by the ABI (TP 13), 18 November 2014

[50] Ibid c86

[51] Ibid c87-8; Written evidence submitted by the Association of Taxation Technicians (TP12), 18 November 2014

> Our new clause, which would simply require the Government to put information into the public domain to allow us to see their thinking and the workings done behind the scenes so that we could understand the situation better, is a mild-mannered request.[52]

In response, Mr Gauke explained why he thought the proposed new clause unnecessary:

> Distributional analysis measures the impact of Government changes to tax and spending. Although the measures in the Bill are clearly taxation measures, they do not, in and of themselves, make individuals materially worse off or better off. They increase the choices available to individuals over how they access their savings and allow people to delay or bring forward their income, but do not alter the amount of savings that they have in aggregate. As the Government set out in paragraph 1.9 of the distributional analysis document accompanying this year's Budget, the distributional analysis
>
> > "shows the impact of changes in government fiscal policy with a direct impact on households, but not of all government decisions."
>
> The tax information and impact notes published at the Budget set out the Government's analysis of the impact of the measures contained in the Bill, including estimates of the costs to the Exchequer, certified by the independent Office for Budget Responsibility, and equalities impacts.
>
> The new clause would require the Government to publish a full behavioural analysis and a financial risk assessment. As I am sure hon. Members will realise, the costing of tax measures can involve an assessment of the behavioural impact of the measure and, in some cases, the capacity for additional tax planning and avoidance behaviour. Those assumptions are certified by the OBR. However, the Treasury considers that the publication of detailed behavioural assumptions can have the potential to affect that behaviour and, as such, is potentially detrimental to policy-making.
>
> The policy costing note published alongside the Budget explains how the costings have been calculated in line with the principles outlined in the Government document, "Tax policy making: a new approach", which was published alongside the June Budget in 2010. The costings of the policy will, as I said in the evidence that I gave to the Committee, be updated at autumn statement, when they have been certified by the OBR. The policy costing note will be published, setting out how the costings have been reached.[53]

He did not think the risk regarding investment in infrastructure should be overstated:

> The point is that annuities will remain the right product for many people. The regular cash flow profile and potential long duration of infrastructure assets will continue to be attractive for backing long-term liabilities such as annuities. As such, infrastructure is likely to remain an attractive investment for institutional investors, including the insurers.[54]

Ms Jamieson's amendment was defeated on division by 10 votes to 7.[55]

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[52] Ibid c88
[53] Ibid c89
[54] Ibid c93
[55] Ibid c95

4.5 Opposition amendment – Pension flexibility: Treasury review

Ms Jamieson tabled a further amendment to require the Chancellor of the Exchequer to publish a review of the impact of the legislation within one year of Royal Assent. This would include the distributional impact, a behavioural analysis, the impact on Exchequer revenues, the use of salary sacrifice arrangements and the purchase of annuities.[56]

She said the guidance guarantee was considered critical to the success of the Bill. However, there were concerns about the timescale for getting it up and running and ensuring its effectiveness:

> It has been suggested—some may think this is unfair—that the first tranche of people who go through the process using the guidance guarantee are effectively the guinea pigs. How much will we be able to learn from that and seek information back from them to find out how useful they found it? How many of them, for example, will be signposted to take regulated advice, and what will they feel about their experiences? Those are the kind of things I hope to capture as part of the process of a review of the legislation.[57]

Furthermore, the suggested 'second line of defence' has not been put in place. It would be important to be able to adapt it in the light of experience.[58] A review would also enable the use of salary sacrifice arrangements to be considered.[59]

Nic Dakin said a review could also help identify signs of mis-selling:

> There are behavioural analysis issues that need looking at in relation to how the guidance guarantee works and how that impacts on behaviour. That is important. Secondly, there is the problem that has been identified on the future impact. Is there a possibility of creating circumstances that result in another mis-selling episode? That would create all sorts of chaos, which would make the Arch Cru example and others of small importance in the grand scheme of things. That is a genuine worry and concern. Analysis of the Bill's behavioural impact would be a safeguard against that. If anything inappropriate was happening or the safeguards were not strong enough, that could be addressed, sooner rather than later, which would be to the benefit of everyone. [60]

Teresa Pearce said a review would help identify emerging risks to individuals:

> There is a risk that a person might pay too much tax, run out of money, purchase the wrong product or leave their spouse with no money should something happen to them. Those are all important issues. A review will show us whether things have gone as we intended. We all hope that opening up the pensions market will work well for the consumer, but, as is the case whenever anything is opened up to the consumer, we know that, as we sit here, people are working out exciting products to sell to people whose knowledge of the market is relatively unsophisticated. It is important that we have more than a single line of defence.[…] We are discussing taxation—this is the Taxation of Pensions Bill—but a large number of people in this country think that pensioners do not pay tax. That is some people's level of understanding. Has the Minister considered any options for public information or advertisements?[61]

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[56] Ibid c95-6
[57] Ibid c99
[58] Ibid c101
[59] Ibid c101
[60] Ibid c102
[61] Ibid c103

Geoffrey Robinson said the government would be held account for regulation of the industry and would therefore need "timely, relevant information."[62]

In response, David Gauke said the proposed new clause was unnecessary:

> First, it would require the Government to preview the distributional impact of the measures in 12 months' time. As I set out when discussing new clause 2 on Tuesday, the measures in the Bill will not have a direct consequential impact on household incomes. Any effects will be driven by the choices individuals make about when to take their pension and in what form. Additionally, household income is not necessarily a reliable measure of pension wealth, especially in the years shortly before retirement. There would be some potential to misrepresent the impacts of the policy if we were to assess it only against the distribution of household income.
>
> With regard to behavioural analysis, the issues I mentioned in relation to new clause 2 remain relevant. The Treasury believes that the publication of detailed behavioural analysis relating to tax measures has the potential to be counter-productive, as it can itself alter behaviour. The tax information and impact note published at Budget already commits the Government to keep the policy under review through the monitoring of information collected on tax returns and tax records.[…]
>
> With regard to the point about salary sacrifice, as the Government response to the consultation stated, and as I mentioned on Tuesday, the Government will closely monitor behaviour under the new system […]
>
> As I said, in terms of the behavioural effects and the impacts on tax revenues, the information will be available in future in the normal way. We plan to continue working with interested parties to ensure that the system remains fair and proportionate. There are continuing discussions between the Government and industry. The discussions will provide the basis for continuous consideration of the way in which the system is working. If the Government see evidence that the new system is being abused, we will not hesitate to address it.
>
> New clause 3 would also require that any published review include any impact the measures contained in the Bill have on the sale of annuities. I believe that would be inappropriate. The changes made by the Bill are not about annuities, or about encouraging savers towards one particular product at the expense of another; they are about increasing choice and flexibility at the point of retirement. The Government have been very clear that they expect annuities will continue to be the right choice for many people at some point in their retirement, because of the security they provide. However, the point of the reforms is that the Government do not wish to dictate what financial products an individual should use during their retirement.
>
> Data on annuity sales will continue to be available through other channels, such as the data published by the Association of British Insurers and publications by individual firms. For the Government to publish further data would be an unnecessary duplication of information in the public domain.[63]

Regarding regulation, he said:

> The hon. Member for Erith and Thamesmead raised the need for a second line of defence should consumers not engage with the guidance service. It is important to recognise that these reforms are designed to give consumers the freedom to choose how they use their pension savings in retirement.

[62] Ibid c105
[63] PBC Deb 20 November 2014 c111-2

> The FCA has made clear that firms should not do anything to dissuade customers from taking up the guidance, and those who choose not to do so will receive information about their options as they do currently, including a clear message that they can shop around on the open market. The Government will continue to work with the regulators to ensure that providers give the right information to consumers. If existing requirements and options need to make that clearer, we are committed to making that happen as quickly as possible.
>
> The last point I would like to address is the possibility of scams, fraud and mis-selling when the new system comes into place. The Government are taking a number of actions to prevent that type of behaviour next year. First, the guidance will promote consumer awareness of scams and give practical tips, such as how to check whether a firm is regulated on the FCA's register.
>
> Secondly, the FCA has a clear objective to protect consumers and an extensive and highly effective toolkit to ensure that they are protected. For example, with regard to mis-selling, the FCA has the power to remove a firm's permission to trade, and to ban the directors of a firm from setting up business in the industry again. It also has the ability to issue unlimited fines. The FCA has recently launched a new high-profile consumer awareness campaign on investment scams, known as "ScamSmart".
>
> Thirdly, to ensure that no one tries to pass themselves off as a guidance provider, the Government have introduced an amendment to the Pension Schemes Bill to make that a criminal offence.[64]

He said there was concern in the industry that the Opposition might change the policy in future:

> I attended a conference yesterday with the industry where some concern was expressed that it indicated that the Opposition were not keen on this additional flexibility or on providing more choice, and tabling the amendments was a precursor, in the event of a future Labour Government, to them removing the choice and flexibility that this Government have given. I reassured the conference that this was merely about the level of scrutiny that one would expect from a diligent Opposition, and that they should not read into it any indication that the Labour party was backsliding in its support of the measures or lukewarm, or that it was preparing the ground to remove the flexibilities in the future.[65]

Cathy Jamieson responded that:

> We have said on numerous occasions, but I will repeat it again, that the scrutiny of this Bill and, indeed, of the Pension Schemes Bill, is not about the straightforward principle of allowing people freedom and choice. It is correct that we exercise due diligence and proper scrutiny to ensure that the Bill is fit for purpose and that we have properly considered all of the issues.[…]The Minister will say that everything is under continuous review, and he knows as well as I do what that means. People will be beavering away in the background on certain things, keeping an eye on them and looking at what is going on; but unless there is a focus, catalyst or trigger to bring them back into the public domain that will not necessarily happen. I do not want a scam or scandal to be the reason for bringing those things back into the public domain, so I am trying to be helpful. I am trying to work with the grain of what the Minister is doing, to

[64] Ibid c114-5
[65] Ibid c116

> ensure that his officials can continue to work on the matter, and to secure a time scale for bringing back information. That is important for monitoring.[66]

The amendment was defeated on division by 10 votes to 6.[67]

5 Report stage and Third Reading

The Bill had its Report Stage and Third Reading in the House of Commons on Wednesday 3 December 2014, immediately after the Autumn Statement. This included updated information on the impact of the Bill (see SN 6891 – section 2.2). The Government also announced how it would change the 'notional income rules' for means-tested benefits (see SN 6891 – section 4.7).

The Government amended the Bill to simplify the information requirements in Part 6 of Schedule 1. Financial Secretary to the Treasury, David Gauke explained:

> It might be helpful if I start by setting out why these information requirements are required. As we have discussed many times during the course of this Bill's passage through the House, when an individual accesses their pension flexibly, their annual allowance for tax-relieved defined contribution pension contributions will reduce from £40,000 to £10,000. That will protect the Exchequer and ensure that the new system cannot be exploited to achieve unintended tax advantages by individuals' diverting their salary into their pension and withdrawing it immediately with tax relief. It is therefore important that individuals understand the tax consequences of saving into a pension after accessing their savings flexibly. For that reason, the Bill placed a new requirement on individuals to tell all their pension providers once they had flexibly accessed a pension. This was intended to ensure that individuals do not use the new system to gain a tax advantage that is not intended. However, the Government have always been clear that they are keen to ensure these requirements are proportionate.
>
> Having considered the issue carefully, we are amending the Bill to provide that people need to tell only the schemes to which they are contributing or that they contribute to in the future. They will also have an extended period of 91 days in which to do so. These changes will make the new system easier for individuals and schemes to comply with, while also ensuring that the new annual allowance is implemented effectively.[68]

The requirement would not apply where a scheme provided defined benefits only. However:

> If the scheme also provides money purchase benefits—for example, if it has a separate AVC section—the requirement can only apply where contributions are made to the AVC section. Defined benefit schemes are excluded as they will not have to send pension saving statements to the individual based on the £10,000 money purchase annual allowance.[69]

Shadow Financial Secretary, Cathy Jamieson welcomed the amendments.[70]

Ms Jamieson moved an amendment (new clause 1) calling for a review by 6 April 2017, detailing the impact of the Bill on Government revenues, with particular reference to opportunities for tax avoidance and national insurance contributions avoidance.[71] She said:

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66 Ibid c119
67 Ibid c124
68 HC Deb 3 December 2014 c384-5
69 Ibid
70 Ibid c386

In Committee, we tried to get more details and figures, and the comments of John Greenwood and others were often quoted, particularly those relating to concerns that the Bill could allow individuals to divert large sums into their pensions through salary sacrifice. Those individuals would then be able to take as much as they wished from that pension in the following year, as 25% would be tax free and the rest would be charged at their marginal rate, with no money deducted through national insurance contributions. Although the introduction of the money purchase annual allowance rules is supposed to prevent that, the reduced £10,000 limit is activated only after the pension has been flexibly accessed for the first time.[…]

The Association of Accounting Technicians has raised concerns about this, saying:

> "In the first year, before the £40,000 allowance is lost, individuals over the age of 55 will still have the scope to save tax and NI on the full £40,000, provided they have the necessary earnings, less their existing pension contributions. Where an individual flushes (passes) an extra £30,000 through pension rather than drawing salary they will achieve a saving of £3,600 in employee NI, more than £1,500 in income tax and, also, £4,140 in employer NI (13.8%) in the first year. A total loss to the public purse of £9,240. The "Freedom and choice in pensions" rules mean this money can be withdrawn immediately if an individual is over 55. This fact means that there will not be clear distinction between salary and pension for this age group."

I have some questions for the Minister about that. Does he agree that the Bill, as it stands, would afford additional scope for tax avoidance of the type outlined? I know we have discussed this matter in Committee, but it is important to probe it until the last possible moment. […]

Taxpayers and employers need to know whether the Government will regard the diversion of salary through pensions as legitimate.[72]

Another Opposition amendment (new clause 2) - would have required a review within 18 months of other issues, such as the impact of the changes on the tax treatment of unused fund at death, a distributional impact of the measures in the Bill, the impact of the Act on the purchase of annuities etc.[73]

For Plaid Cymru, Hywel Williams as about the "impact of the changes introduced by the Bill specifically on the housing market and introduce measures to rectify any problems, should it become apparent that there are negative consequences."[74] Geoffrey Robinson said this was an "unknown area where there is a fear of scams and abuses emerging—mis-selling and such things that have characterised so much of the industry in the past."[75] Toby Perkins asked about the risk of people who had thought they had provided for themselves in later life finding out that their investments had gone wrong.[76]

David Gauke explained why he thought the amendments were unnecessary:

First, on considering new clause 1 and the parts of new clause 2 that relate to Exchequer revenues, it is important to note that the Government have today published estimates of the Exchequer impacts of the policy as a whole. These costings, which

[71] HC Deb 3 December 2014 c363
[72] HC Deb 3 December 2014 c361-3
[73] Ibid c361
[74] Ibid c369
[75] Ibid c371
[76] Ibid c373

> have been certified by the independent Office for Budget Responsibility, cover all the changes we have made to the policy since Budget as a result of consultation.[…]
>
> The Government have, therefore, already published the information the two new clauses seek on the Exchequer impacts of the various aspects of flexibility, and all that information has been certified by the independent OBR. In addition, the Government have already committed to keeping the policy under review, through the monitoring of information collected on tax returns and tax records, and HMRC regularly publishes data on tax receipts reflecting any impact on the Exchequer. Any such impacts will be reflected in forecasts at fiscal events.[77]

Regarding the impact of the Bill on the purchase of annuities, he said:

> […] the Government do not believe it appropriate to mandate that individuals should use their lifetime savings to purchase any one specific financial product. As I set out in Committee, data on the sale of annuities will continue to be available through other channels—the data published by trade bodies and publications by individual firms, for example—and there is no need for the Government to duplicate this.[78]

Regarding the impact on the housing market, he said:

> As part of the new regulatory framework for financial services, the Government have introduced the Financial Policy Committee to ensure that risks stemming from the housing market are identified and early mitigating action taken, if required.[79]

The guidance guarantee was being set up to help people understand the implications of their choices:

> The guidance will help consumers to understand the tax implications of their choice of pension, and in addition, the Financial Conduct Authority has published near final rules that will require providers to supply their customers with a description of the possible tax implications when they apply to access their pension funds.
>
> On extortionate draw-down charges, the FCA's retirement income market study will be published shortly. In June, the FCA expanded the scope of this study to include consideration of products in the new flexible landscape and to identify any competition risks and potential consumer detriment. The guidance guarantee will be relevant here.
>
> It was suggested that people might be charged too much tax without realising it. As with all PAYE income, the tax position will be reconciled at the end of the tax year. All the income received by an individual that was taxed under PAYE will be brought together, and the correct tax will then be calculated. If there was an overpayment, the extra amount will be repaid, and if there was an underpayment, HMRC will contact the individual. People will not be subject to self-assessment solely because they have flexibly accessed their pensions, nor will they have to claim a refund in order to receive it.[80]

On the implications for entitlement to means-tested benefits and help with the costs of social care, he said

> New regulations and statutory guidance on the *Care Act 2014,* which were published on 23 October, include details about the charging rules for care and support. Today we

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[77] Ibid c366
[78] Ibid c377
[79] Ibid c378
[80] Ibid c378-9

announced a change in the rules for people above pension credit qualifying age who claim means-tested benefits. The notional income amount applied to pension pots that have not been used to purchase an annuity will be reduced from 150% to 100% of the income of an equivalent annuity—or the actual income taken, if that is higher—in line with the rules for care and support.[81]

New clause 1 was defeated in division by 209 votes to 292.[82]

The House then proceeded to give the Bill its Third Reading. The Minister summarised the amendments the Government had made to the Bill since its introduction:

> The Government have made a number of minor and technical amendments to the Bill to ensure that it works as intended. The most substantive changes have been to the taxation of pensions at death, to ensure that that taxation remains fair and appropriate under the new system. The changes will allow individuals who die with pension funds remaining to pass those funds on to anyone they choose. The funds can be paid tax-free if the individual dies before the age of 75; if they die having reached that age, and the funds are paid out as a pension, they will be taxed at the beneficiary's marginal rate—or at 45%, if the funds are paid as a lump sum. The aim of the changes is to ensure that individuals who have made sacrifices to save over the course of their life can pass on their pension savings without worrying about excessive tax charges after they die. They also preserve the incentive for people to keep money in their pension, as there will not be the fear of their beneficiaries being hit by a 55% tax charge.[83]

He mentioned that in the Autumn Statement, the Government had announced that the tax treatment of joint life and guaranteed term annuities would also change. It said:

> **1.222** The government has now decided to go further. **From April 2015, beneficiaries of individuals who die under the age of 75 with a joint life or guaranteed term annuity will be able to receive any future payments from such policies tax free. The tax rules will also be changed to allow joint life annuities to be passed on to any beneficiary.** These changes mean that people will no longer have to worry about their pension savings being taxed at 55% on death.[84]

This would apply to first payments made to a beneficiary after 6 April 2015:

> This will apply to first payments made to a beneficiary after 6 April 2015. For the 2015-16 tax year, if an individual dies over the age of 75 and their remaining pension is paid out as a lump sum death benefit, a charge of 45% will apply. This will be reduced to marginal rate from April 2016. Payments from joint life or guaranteed annuities to beneficiaries including non-dependants, can be paid tax free from April 2015 where the original policyholder dies under the age of 75. This will apply to joint life and guaranteed annuities where the first payment is made to a beneficiary after 6 April 2015.[85]

Mr Gauke explained that these changes would be "legislated for in due course, although not through this Bill."[86]

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[81] Ibid c379
[82] Ibid c380
[83] Ibid c393
[84] HM Treasury, Autumn Statement 2014, Cm 8961, December 2014
[85] HM Treasury, Autumn Statement 2014 – policy costings document, December 2014
[86] HC Deb 3 December 2014 c396

Ms Jamieson said the Opposition supported the principle of the Bill. Until the reforms took effect, it would be difficult to measure the Bill's performance against the three tests the Opposition had set for the reforms (the advice test to ensure that savers get the right guidance, the fairness test to ensure that there are decent products for low and middle income savers, and the cost test to ensure that the reforms do not result in extra pressures on the state). It therefore reserved judgment on how it would work. She noted that the Office for Budget Responsibility (OBR) had given the costings for the pension flexibilities a 'very high' uncertainty rating:

> The yield over the scorecard period—and the resulting costs in the longer term—depends on take-up and on other behavioural responses. Some people will temporarily increase pension saving in order to benefit from tax-free lump sum withdrawals. It is possible that funds will be redirected from annuities and into other assets, such as other financial products or housing. It is also possible that such funds could be used to finance consumer spending.[87]

She said this was what the Opposition had been "highlighting throughout the Bill proceedings, and exactly why we felt it was important that a review was built into the process."[88]

6 House of Lords

The Bill (HL Bill 66) was given its First Reading in the House of Lords on 3 December 2014, when it was endorsed as a Money Bill.[89] The *Parliament Act 1911* charges the Speaker of the House of Commons with certifying whether a Bill is a Money Bill. If a Bill is so certified, the 1911 Act restricts the length of time the House of Lords has to consider it to one month; and allows for a Money Bill passed by the Commons to be presented for Royal Assent, after that month has elapsed, even if the House of Lords does not agree to it. A Money Bill is one that deals with national taxation, public money or loans and their management. [90] The Bill had its Second Reading and remaining stages in the Lords on 16 December 2014.[91]

The *Taxation of Pensions Act 2014* received Royal Assent on 17 December 2014.

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[87] Ibid c396; OBR, Economic and fiscal outlook, December 2014. See also, p217, para A.6
[88] Ibid c395
[89] HL Deb 3 December 2014 c1384
[90] *Parliament Act 1911*, section 1; Parliament website – Glossary. Money Bills
[91] HL Deb 16 December 2014 c164