HM Treasury

# Budget 2014: greater choice in pensions explained

## People’s pensions are hard-earned over years of work. It is only right they have the freedom to choose how and when they access them during retirement.

At the moment people don’t have full flexibility when accessing their defined contribution pension during their retirement – they are charged 55% tax if they withdraw the whole pot.

We’re announcing that from April 2015, people aged 55 and over will only pay their marginal rate of income tax on anything they withdraw from their defined contribution pension – either 0%, 20%, 40% or 45%.

## How the current system works

The government has already helped increase the security of people’s income in retirement by introducing automatic enrolment into workplace pensions and the triple lock guarante. But the current system is complicated and restricts people’s choices.

Under the current system, there is some flexibility for those with small and very large pots, but around three-quarters of those retiring each year purchase an annuity.

**Pension pot options**

**Currently, you can take up to 25% of your pension pot tax-free. With the rest, you have 4 options.**

If you withdraw all your money then you are charged 55% in tax

- If you are aged 60 and over and have overall pension savings of less than £18k you can take them all in one lump sum – this is trivial commutation ...
- A ‘capped drawdown’ pension allows you to take income from your pension, but there is a maximum amount you can withdraw each year (120% of an equivalent annuity) ...
- With ‘flexible drawdown’ there’s no limit on the amount you can draw from your pot each year, but you must have a guaranteed income of more than £20k per year in retirement.
- But three quarters of people buy an annuity – an insurance product where a fixed sum of money is paid to someone each year, typically for the rest of their life.

Regardless of your total pension wealth, if you are aged 60 or over, you can take any pot worth less than £2k as a lump sum, as this classifies as a ‘small pot’.

## We plan to overhaul the system completely

From April 2015, from age 55, whatever the size of a person's defined contribution pension pot, we propose that they'll be able to take it how they want, subject to their marginal rate of income tax in that year. 25% of their pot will remain tax-free.

There will be more flexibility. People who continue to want the security of an annuity will be able to purchase one and people who want greater control over their finances candrawdown their pension as they see fit. Those who want to keep their pension invested and drawdown from it over time will be able to do so.

To help people make the decision that best suits their needs, everyone with a defined contribution pension will be offered free and impartial face to face guidance on the range of options available to them at retirement.

The government has published a consultation on these changes alongside the Budget.

## But in the meantime, from 27 March 2014 ...

We're increasing the amount of overall pension wealth you can take as a lump sum from £18k to £30k.

And we're reducing the amount of guaranteed income needed in retirement to access flexible drawdown from £20k per year to £12k per year.

We're also increasing the maximum amount you can take out each year from a capped drawdown arrangement from 120% to 150% of an equivalent annuity.

We're increasing the size of a small pension pot that you can take as a lump sum, regardless of your total pension wealth, from £2k to £10k.

We're also increasing the number of personal pension pots you can take as a lump sum under the small pot rules, from two to three.

## Who will benefit

The changes coming into effect on 27 March will mean around **400,000** more people will have the option to access their savings more flexibly in the financial year 2014-15.

From April 2015, the **320,000** people who retire each year with defined contribution pensions will have complete choice over how they access their pension.