After the dust has settled: Budget 2023 explained

21st March 2023

With the dust now starting to settle on the Budget announcements from last week, we can start to see the impact of the changes and sadly the politicisation once again of pension rules.

The intention behind the Chancellor’s announcement was to encourage early retirees, particularly medical professionals, back into the workplace and to not penalise workers who want to continue to work by disincentivizing pension savings. While the changes were generally targeted at the medical profession, there is a skills shortage across all industries that won’t be entirely solved through changes to the pension system.

There are also many reasons why, and often with our encouragement, people choose to retire early, a change to pension rules will not be enough to change that decision.

So for certain, we know that:

- The Lifetime Allowance tax charge will not apply from 6th April 2023.
- From 2023/2024 the Lifetime Allowance will be abolished.
- Tax Free Cash is to be restricted to £268,275 but protected for people with Lifetime Allowance protection (see below).
- The Annual Allowance will increase to £60,000 (gross) so more can be paid into pensions unless you are caught by the Tapered Annual Allowance.
- The Carry Forward facility will remain in place so people can still catch up on missed contributions.
- The Tapered Annual Allowance is a reduced Annual Allowance based on the level of income you have will still apply but will taper to £10,000 (gross), not £4,000 (gross). The taper of the Annual Allowance is £1 for every £2 the Adjusted Income Threshold is above £260,000.
- The Adjusted Income Threshold is the income measurement where the amount you can contribute to your pension decreases and consists broadly of all taxable income and pension contributions, and once you have reached an income of £360,000 your Annual Allowance will have reduced to £10,000 gross.
- The Money Purchase Annual Allowance (MPAA) will also increase to £10,000 (gross). This is the amount you can continue to contribute to a pension after you have crystallised your benefits.

Clarity on the impact on Lifetime Allowance and Lifetime Allowance protections

HMRC has recently confirmed that the Budget proposals to scrap the Lifetime Allowance will not harm people who hold Enhanced Primary or Fixed Protection. Essentially, those with Lifetime Allowance Protections will be able to keep their higher 'Tax Free Cash' amounts ***and*** make further pension payments should they wish to do so. We expect there to be more detail on this as time passes, as the application of these rules may be complex.

Annual Allowance

The increase to the Annual Allowance has to also be welcomed because it gives savers a greater scope for contributions than was previously the case. Where eligible, contributions of up to £180,000 (gross) can now be made to a pension fund in one lump sum if you have unused allowances from previous years.

For people with Defined Contribution pensions, the amount of contributions paid can be easily managed and the risk of breaching these limits controlled.

However, for people with Defined Benefit arrangements, controlling the impact is difficult. 'Input amounts' are calculated to a formula, which can be impacted significantly by pay rises and inflation. Raising the allowance to £60,000 (gross) will give many people more relief from the taxes, but unfortunately, I expect that there will still be people in Defined Benefit plans that will get caught out.

'Opting' back into pension schemes

There will be a number of people who have opted out of pension schemes due to these taxes who might now be considering whether to opt back in. This is unlikely to be a straightforward decision. Some of the schemes that would have been opted out of, may no longer be open and therefore the terms of the opt in will be different. It is therefore important that each case is considered on its own merits.

The response from the Labour Party

The changes announced by the Chancellor are well intentioned and aim to keep people in work or encourage them to return to work; especially in the NHS, this should be welcomed. However, there is no denying that the policy also helps the wealthy who can now draw benefits and pay a lower overall rate of tax than was previously the case.

The Labour Party has said that it will reverse the changes if they win the next election, and instead introduce a more targeted measure for doctors but we do not yet know how this will look.

However, what this does show is that once again pension planning is becoming overly politicised. As advisers all we want is clarity of rules and confidence in the system so that we can give the best possible long-term advice without always having to consider how different politicians may change the rules as they enter power.

The proposed reversal from The Labour Party will likely encourage the opposite behaviour from what the Chancellor had intended i.e. fast forward of retirement or drawing of benefits so as to take advantage of the new rules in what might be only a small window of opportunity.

Inheritance Tax treatment

There were no changes in the Budget that targeted the attractive treatment of pension funds from an Inheritance Tax perspective. Most pension funds still remain outside of your estate and the rules on death before or after age 75 have not changed. However, this is definitely one area that a Labour government could target.

Portfolio balance

We have always considered that it is sensible to have balance in your portfolio so you are not overly exposed to one arrangement or set of rules. Making savings into pensions has always been hugely efficient from a tax perspective both on the way in, on the way out and on death but there is always risk of political interference and rule changes. This is why it is important to maintain a balance in the portfolio by ensuring that you are investing in other tax efficient vehicles to provide a combination of tax efficiency, flexibility and access so that any significant rule or tax changes will not impact the financial planning too much.

What didn't happen?

There were rumours prior to the budget that the tax rates paid for Capital Gains Tax could change and potentially be brought in line with income tax; this has not happened, meaning that rates will remain at 10% and 20% for investments and 18% and 28% for property. This is good news following the negative changes to the CGT allowances in the last Budget statement.

However, and as has been the case for a number of years now, there has been no indexation to the general income tax allowances meaning that more and more people are paying more tax each year as a result of fiscal drag. This just emphasises the need to carefully plan your finances to ensure you take advantage of all the allowances and tax privileged savings options that are available to you.

Final words (for now)

The changes proposed, whilst welcome, do create some further complexities in the planning and, in the absence of the detailed new rules, we are still considering the implications for people. There could be some time critical decisions that will need to be made in the next 12 months and we will provide guidance on this to everyone in a timely fashion.

We would guard against taking any precipitous action until the finance bill is published, normally in July, when the detailed rules will be known.