The government is introducing the most radical changes to pensions in almost a century.
The changes were initially proposed by the Chancellor in his March Budget. The Government has now confirmed those changes and provided further details (21 July 2014).

Here we give the basic facts and explain how they might affect you.

CHANGE 1: Flexible access to pensions from age 55 (From April 2015)

What is changing: From April 2015 pension investors aged at least 55 will have total freedom over how they take an income from their pension. They could even take the whole fund as a lump sum if they so wish. They will then be able to spend, invest or save it as they prefer. The first 25% will be tax free. The rest will be subject to income tax at your highest marginal rate. So if you are a basic-rate (20%) taxpayer, any income you draw from your pension will be added to any other income you receive (e.g. your salary) and this could push you into the higher (40%) or even top-rate (45%) income tax bracket.

You can choose to take the pension out in stages, rather than in one go, which could help you manage your tax liability. It should also be possible to take the tax-free cash straightaway and the taxable income at a later date.

Who will be affected: Anybody with a defined contribution pension – e.g. individual or group personal or stakeholder pensions, Self Invested Personal Pensions (SIPPs), some Additional Voluntary Contribution (AVC) schemes, etc. – could benefit. Investors aged 55 or over in April 2015 should be able to take advantage of the increased flexibility straightaway.

CHANGE 2: Pension income (drawdown) restrictions to be abolished (From April 2015)

What is changing: One of the options investors have had at retirement is to draw an income directly from their private pension fund, known as income drawdown. There are currently limits on how much most people can draw each year, known as the Government Actuary's Department (GAD) maximum. From April 2015 these limits will be scrapped. Investors will be able to draw as much income as they like.

Using income drawdown, your pension fund remains invested and under your control. You choose how much income to take, and where to invest. Income drawdown allows you to keep your options open and is very flexible both when you take an income and when it is passed on to heirs. However, with this increased flexibility comes the real risk of running out of money in retirement. It is a higher-risk option as, unlike a secure income (annuity) where the insurance company takes on that risk, with drawdown the responsibility rests with you. Poor investment performance or taking excessive income will reduce your income and in the worst case scenario it could run out.

Who will be affected: Anybody who has a defined contribution pension – e.g. individual or group personal or stakeholder pension, Self Invested Personal Pensions, Additional Voluntary Contribution schemes, etc. – could benefit. Investors aged 55 or over in April 2015 should be able to take advantage of the increased flexibility straightaway. Investors already in income drawdown prior to 6 April 2015 will be able to move to the new unlimited regime (i.e. draw more income than the current GAD maximum). However, they will then be restricted on how much they can contribute to pensions in future (see change 3 below).

Change 3: New restrictions on how much you can contribute (From April 2015)

What is changing: If you take any income from your pension (in addition to any tax-free cash) after April 2015, you may still be able to make pension contributions, but only up to a reduced annual allowance of £10,000 a year. This includes employer contributions and pension benefits being built up in final salary schemes, which can be surprisingly large.
There are two exceptions:

1. If your pension is worth less than £10,000. In this case, you will be able to make withdrawals from three small personal pots and unlimited small occupational pots worth less than £10,000 each without being subject to the new £10,000 allowance;
2. If you go into capped drawdown before April 2015 and your withdrawals after April 2015 remain within your drawdown limit. In this case you will not be subject to the new £10,000 allowance.

This is being introduced to stop people having their salary paid directly into a pension and effectively receiving 25% tax free and avoiding national insurance on employment income.

Who will be affected: Anybody who has a defined contribution pension – e.g. individual or group personal or stakeholder pension, Self Invested Personal Pensions, Additional Voluntary Contribution schemes, etc. – worth more than £10,000 and takes income from it after April 2015 will be affected. Investors already in flexible drawdown before April 2015 will be able to make contributions of up to £10,000 a year (they are not currently allowed to make any contributions).

This will not affect you if you have not started drawing your pension or if you buy an annuity. You will still be subject to the £40,000 annual allowance and current pension contribution rules.

Change 4: Access to impartial guidance (From April 2015)

What is changing: In his Budget speech, George Osborne announced his intention that everyone should have free guidance to help them make sense of their options at retirement. It has now been confirmed this service will be provided by consumer-facing, impartial organisations such as The Pensions Advisory Service (TPAS) or the Money Advice Service (MAS). There will be no charge and it will be offered through a range of channels, including web-based, phone-based and faceto-face. Your pension provider will be required to tell you about the impartial guidance.

Who will be affected: Anybody taking retirement benefits after April 2015.

Change 5: Transferring a defined benefit pension (e.g. final salary) (From April 2015)

What is changing: Anyone with a defined benefit (e.g. final salary) pension will be able to take advantage of the new rules and make unlimited withdrawals. To do so, they will have to transfer to a defined contribution pension (e.g. a SIPP). But as you could lose very valuable benefits, you will have to receive Independent Financial Advice first.

Who will be affected: Anybody with a defined benefit pension, wishing to take advantage of the increased flexibility after April 2015. It will no longer be possible to transfer from most public sector pension schemes.

Change 6: Retirement ages to increase (From April 2015)

What is changing: The age at which you can draw your pension, currently 55, is set to increase. It will be 57 from 2028 and from then increase in line with the rise in the State Pension age. It will remain 10 years below the State Pension age. This will not apply to Public Sector Pension Schemes for Firefighters, Police and Armed Forces.

CHANGE 7: Possible fall in the tax paid when you pass on your pension (from last quarter of 2014)

What is changing: In March 2014, the Chancellor promised to review the tax paid on pension lump sums when you die. If you are in drawdown, or you are 75 or older, any lump sum paid to your beneficiaries is currently taxed at 55%. This has not been reviewed yet, but the Chancellor still believes this is too high and has promised a review later in 2014.

If you die before you go into income drawdown or buying an annuity, and before age 75, the entire pension fund can normally be paid to your beneficiaries free of a tax charge.