Budget 2025: the good and the bad for pension schemes and members

Rachel Reeves's Budget was relatively benign for pension schemes and members. But the salary sacrifice cap has potential negatives and the run-up again felt like open season on pension savers.

After months of unsettling speculation, briefings and U-turns, the Chancellor finally unveiled her Budget in the House of Commons yesterday. There were two main announcements affecting pension schemes and members:

The decision to cap salary sacrifice at £2,000 a year
Indexation of pre-1997 pensions for Pension Protection Fund (PPF) and Financial Assistance Scheme (FAS) members
The first measure was widely expected; the second, less so. Both were far more welcome than ideas floated before the Budget such as cutting the tax-free sum allowance or making savings from tax relief on pension contributions. More on this later.

Let's take the two policies in turn.

1. Salary sacrifice

Salary sacrifice lets employers offer staff a de facto pay cut and instead channel that income into their pension or towards another benefit such as childcare or a bike for commuting. As a result, both parties pay less national insurance.

As expected after heavy trailing, the government has capped the amount anyone can sacrifice at £2,000 a year. Previously, minimum wage rules aside, there was no limit on the amount savers could sacrifice into their pensions.

On the plus side for the Treasury, this move will raise more than initially expected. The Office for Budget Responsibility estimates the cap will raise £4.7 billion in 2029-30 and £2.6 billion in 2030-31. And it's easy to see why Reeves targeted salary sacrifice.

Many people don't understand salary sacrifice, and the government has raised examples of potential abuse such as people buying expensive bikes that aren't used to cycle to work. But when it comes to pensions, salary sacrifice was simply a way to get people saving more – and this is one of the government's goals.

The new limit, delayed until April 2029, is seen as a halfway house, affecting more affluent members who are in a position to put more than £2,000 into their pension in a year. But there are likely to be many exceptions.

Salary sacrifice also includes bonuses. A member's normal contributions may not exceed the £2,000 but some people may be sacrificing their bonuses into the scheme. Someone earning, say, £25,000 receiving a 10% bonus would have £2,500 to put into their pension – and their employer might make this an attractive option with matched contributions.

You don't have to be a big earner to be affected by this change, and it's easy to see how pension outcomes could be made worse for plenty of people.

Delaying the cap until 2029 was a surprise, and it raises suspicions that the Treasury isn't sure how to implement it. Employers have more than three years to come up with new ways to make pensions serve their recruitment and retention goals, and we'll wait to see if the policy will work.

1. Indexation of some pre-1997 pensions

The Chancellor's announcement that she would index pre-1997 pensions in the PPF and FAS is good news for members who lost out when their employers went insolvent. Campaigners have pressed the case for this change for many years, and the PPF and the Society of Pension Professionals have welcomed the decision.

However, pensioners in the PPF and FAS aren't the only members who have been calling for their pensions to be indexed. This measure could put further pressure on trustees of other schemes that similarly aren't protected against inflation.

After a long bout of high inflation, members of large occupational schemes are already lobbying MPs for their benefits to be indexed, and this measure could encourage them to press harder with many schemes in surplus.

This is a complex subject and most trustees will be cautious about responding to these calls, often because they don't want to set a precedent or a potentially confusing expectation for members. Equally sponsors and the government were looking to spend this money in ways to drive their businesses and the economy.

We looked at the effects of high inflation on pension scheme members in this recent insight and discussed how trustees might respond. After Reeves's announcement, trustees of schemes that aren't fully indexed would be wise to prepare for further enquiries by making sure they understand their scheme's position and preparing clear, empathetic member communications.

Pre-Budget rumours risk undermining confidence in pensions

Finally, let's look at the effect of what didn't happen in the Budget. When Reeves announced the date of her speech we warned that a round of speculation and kite-flying akin to what happened before her first Budget could undermine confidence in pensions.

The Office for Budget Responsibility is holding an inquiry into how it published its data before the Chancellor's speech. But for pension savers the stream of pre-budget speculation about pensions taxation was far more damaging.

If anything, the rumour mill was more intense this time because Reeves seemed to be in a deeper fiscal hole and she left almost three months between announcing the Budget and delivering it. Ideas floated included cutting the tax-free lump sum allowance and changing tax relief on contributions.?It wasn't until 11 November that the Treasury briefed that changes to the tax-free lump sum allowance were off the table.

Some people will already have made hasty financial decisions. In September the Financial Conduct Authority revealed a jump in withdrawals of tax-free lump sums as savers prepared for the Budget. And many more may now wonder if their long-term plans could be disrupted in the future.

Each time the government tinkers with taxing pensions or trails potential cuts to allowances, it risks undermining pensions as the best way to save for retirement. Pensions are a long-term financial arrangement and shouldn't be subject to short-term speculation before every Budget.

Today, Reeves didn't rule out further tax increases in this parliament. This is probably sensible, but pension savers need more reassurance that the government is on their side.

purpose. We strongly recommend seeking appropriate professional advice tailored to your specific circumstances before making any decisions?based on this information.

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