

## Pensions Reform Update – 27 October 2010

### Introduction

Following the Spending Review on 20 October, the Review Committee issued its report on Pension Reform on 27 October. The Government has now made decisions on all the key points and it is likely these will take effect from 6 April 2011, but they will have an immediate impact on pension planning and advice.

### Key Decisions

- Anti-forestalling will end on 5 April 2011 as expected.
- Labour's original plans for tapering tax relief for high earners will be scrapped.
- A reduced Annual Allowance (AA) of £50,000 from April 2011 will apply. In future this may be subject to indexation increases but not until after 2015/2016.
- Reduction of the Lifetime Allowance (LTA) from £1.8m to £1.5m from April 2012.
- Review (in November 2010) of potential to allow individuals flexibility to pay large AA tax charges from their Pension Scheme.
- Allowing a form of carry-forward of up to three years previous unused allowances. This is intended to ease or smooth out large one-off spikes in accrual that exceed the AA in a single year, for those on moderate incomes. The carry-forward limit for 2008/2009, 2009/2010 and 2010/2011 will be £50,000.
- Allowing Schemes and Employers to manage one-off spikes in pension contributions or accrual through flexible scheme design and other mechanisms, whilst ensuring these do not fall foul of anti-avoidance principles.\*
- Valuing final salary Defined Benefits (DB) using an increased flat factor of 16. (The current flat factor is 10.) In partial mitigation benefits already accrued can be revalued before applying the factor. This ensures parity with deferred members who are exempt from the AA test.
- Replacing the flat AA tax charge on excess contributions (currently 40%) with a 'tailored' tax charge that effectively reclaims tax relief at marginal rates and reduces tax relief to 0% on contributions above £50,000.
- Full tax relief at the marginal rate (up to 50%) on pension contributions within the reduced AA.
- Introducing exemptions from the AA test for death and ill-health.
- No exemption from the AA test on redundancy.
- Removing the 'final year, all benefits coming into payment' exemption from the AA tax charge.
- Removing the exemption from the AA test for those with enhanced protection.
- Pension Input Periods (PIPs) will not be aligned to the tax year. There will be transitional rules effective from 14 October 2010 for those who have already made, or will make, contributions greater than £50,000 in a PIP ending in 2011/2012.
- Some Transitional protection for those with pension values already above the reduced LTA or who have made plans based on a LTA of £1.8m.\*
- Further protection for those relying on existing transitional protection rules.\*
- Breaking the LTA link for triviality. The limit will remain at £18,000 (previously 1% of the LTA).
- Provision of information requirements for both Employers and Schemes. This includes requiring schemes to report pension input amounts to members. This will aid correct and timely completion of self-assessment tax returns.\*
- Anti-avoidance legislation for Employer Financed Retirement Benefit Schemes (EFRBS) and Employee Benefit Trusts (EBTs) to ensure that they do not become more attractive, as a means of remunerating or pensioning the highly paid, than any other method.\*

\*This may be subject to further consultation and more information to follow.

## Impact of Pensions Reform – 27 October 2010

### What do we know?

- Practically no change for anyone paying in less than £50,000 a year to a Pension Scheme.
- The AA is still £255,000 for PIPs ending in the 2010/11 tax year.
- For PIPs commencing pre 14 October 2010 and ending in the 2011/2012 tax year, the transitional rules will allow up to £255,000 to be paid in without breaching the AA rules. But only £50,000 can be paid on or after 14 October or an AA charge will follow – unless the member can rely on carry forward rules to mop up the excess.
- Employer contributions also count towards the £50,000 AA. Where these take the total contributions above £50,000, they could cause a tax liability for the scheme member of as much as 40% or 50% of the amount paid in.
- Likewise DB Scheme accrual can trigger tax charges on scheme members. This is particularly acute for those benefiting from any one or more of long service, higher salaries and accelerated accrual.
- It is still possible to make personal contributions of up to 100% of relevant UK earnings. But, effectively, no tax relief will be given where such contributions exceed £50,000 or such higher amount as is possible under carry forward rules – see below.
- Those ‘high earners’ with relevant income of greater than £130,000, who are caught by the anti-forestalling rules, can still only receive full higher rate tax relief up to the higher of their Protected Pension Input Amount and the Special Annual Allowance for contributions made up to 5 April 2011, when Anti-forestalling ends.
- PIP end dates can still be adjusted to end sooner than 12 months after commencement but not retrospectively – the new end date must be in the future. Remember: no more than one PIP per pension arrangement can end in any one tax year.
- To use the carry forward rules there must have been at least some pension input in the annual allowance year being carried forward for the client. Carry forward won’t be possible for any year when the individual is not a member of a Registered Pension Scheme.
- When applying carry forward the earliest year’s unused allowance is applied first to mop up any excess over £50,000.
- Under DB Schemes carry forward involves reworking the member’s pension input amount for the appropriate year using the 16:1 method.
- For DB schemes, revaluation of existing accrual will be in line with the Consumer Prices Index (CPI) for the September before the tax year in which the annual allowance is tested. For 2011/12 that means September 2010’s CPI is used to revalue benefits accrued to April 2011.
- Carry forward can be used immediately as long as the client’s PIP already ends in the 2011/12 tax year.
- There is no need to make a claim to HMRC to use the carry forward facility or report via self-assessment that carry forward was used.
- Anyone wishing to take all their benefits (other than in serious ill-health) and avoid the AA test must do so by 5 April 2011.

### What do we need clarified?

- Can high earners who were caught by Anti-forestalling use carry forward in 2011/2012 and subsequently ‘catch up’ fully tax relievable contributions for the two previous tax years when they were restricted to the Special Annual Allowance? The likely answer is No.
- Is it possible to start a new pension arrangement and PIP after 14 October 2010 and bring it to an early close (before 6 April 2011) to make full and final use of the AA for 2010/2011 of £255,000?
- How will the new LTA and protection rules impact on pension planning for the wealthy?

More information and examples of the new rules working in practice is currently available via the following links:

<http://www.hmrc.gov.uk/budget-updates/index.htm>

[http://www.hm-treasury.gov.uk/d/wms\\_pensionstaxrelief\\_141010.pdf](http://www.hm-treasury.gov.uk/d/wms_pensionstaxrelief_141010.pdf)

[http://www.hm-treasury.gov.uk/d/restricting\\_pensions\\_summary141010.pdf](http://www.hm-treasury.gov.uk/d/restricting_pensions_summary141010.pdf)

#### IMPORTANT NOTICE

This is Forrester-Hyde Ltd’s understanding of the Law at 16 November 2010. Every effort has been taken to ensure the accuracy. Forrester-Hyde Ltd does not accept any liability in relation to the contents of this document.

Forrester-Hyde Ltd observes high standards of integrity and fair dealing and at all times act with due skill, care and diligence. This requires our firm seeking from clients we advise information about their circumstances and investment objectives, which might reasonably be expected to be relevant in enabling our firm to fulfil its responsibilities.

### **Forrester-Hyde Ltd**

Authorised and Regulated by the Financial Services Authority

19 Clifftown Road, Southend-on-Sea, Essex SS1 1AB

Tel: 01702 432532 – Fax: 01702 431466

Email: [Postmaster@forrester-hyde.co.uk](mailto:Postmaster@forrester-hyde.co.uk)

Web: [www.forrester-hyde.co.uk](http://www.forrester-hyde.co.uk)

PENSIONSREFORM/02

16.11.2010 – NKFH

E. & O.E.