Pension Tax Relief Changes
Warwickshire Pension Fund

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- 11 September 2015

What will be covered....

- Trip down memory lane
- Annual Allowance
  - The current position
  - Example calculations (Inc Carry Forward Allowance)
  - Payment Options
  - 2014 onwards
- Life Time Allowance
  - Calculations
  - Protections
  - 2014 Onwards

What will be covered continued.

- Budget Updates
- New Consultations
- The next steps

A trip down memory lane

Pre April 2006

- Employee contribution restrictions
- Benefits limited on cessation
- Earnings cap in place

A

Day

Post April 2006

- Tax ‘Simplification’
- Removal of previous restrictions
- Introduction of Annual and Lifetime Allowance
- Thresholds – not limits

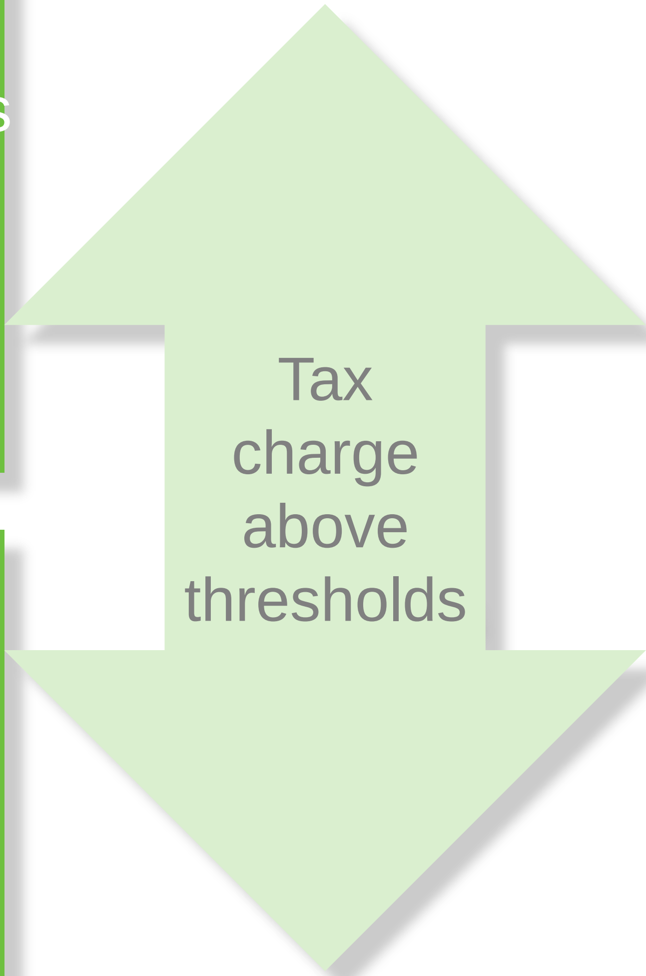
Tax Free Thresholds

Annual Allowance (AA)

- Increase in capital value of benefits
- Yearly
- Factor of 10
- @ 31 March 2011 £255k

Lifetime Allowance (LTA)

- Total capital value of benefits
- On retirement (generally)
- Factor of 20
- @ 31 March 2012 £1.8m



Annual Allowance

2015 tax regime - summary

- Effective from - year to 31 March 2015 for LGPS
- Reduced to £40,000 (April 2014)
- Allowance for the revaluation of previous years' benefits in line with CPI
- Flat factor of 16 used to value increase in DB accrual
- Carry forward 3 years of unused allowance
- Full tax-relief up to the Annual Allowance (marginal rate charge above)

Example 1 – Above CPI pay increase
(Maybe one day....)

- Assumptions:
  - 23 years' pensionable service at March 2015
  - Pay in Year 1 £80,000
  - Pay in year 2 £85,000
  - CPI 2%

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Calculation of the value of benefits

Step 1 – Start of PIP

- 1 April 2014
- Pay = £80,000
- Service
  - 16 years pre March 2008 (80ths)
  - 6 years post March 2008 (60ths)
- Benefits Payable
- Pension £24,000
- Lump sum £48,000

Step 2 – End of PIP

- 31 March 2015
- Pay £85,000
- Service
  - 16 years pre March 2008 (80ths)
  - 6 years post March 2008 (60ths)
  - 1 Year Post April 2014 (CARE)
- Benefit Payable
- Pension £27,235
- Lump sum £51,000

Calculation of pension growth

Step 3 – Compare for growth

		Incl. CPI
Pension at start of PIP	£24,000	(£24,480)
Pension at end of PIP	£27,235	
Growth in excess of 2%	£2,755	(A)
Lump sum at start of PIP	£48,000	(£48,960)
Lump sum at end of PIP	£51,000	
Growth in excess of 2%	£2,040	(B)

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Calculation of pension growth

Step 4 – Apply factor

Growth in pension	£2,755	(A)
Growth in lump sum	£2,040	(B)
Flat related factor	16	(C)
Growth (A x C) + B =	£46,120	
Excess subject to tax charge	£ 6,120	

Calculation of tax rate to apply

Step 5 – Calculate marginal tax rate

Gross income	£85,000
Less contributions	£ 6,555
	£78,445
Plus excess over £40,000	£ 6,120
Total net income	£84,565

- As total income is below £150,000 (45% tax threshold) tax charge is 40%

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Calculation of tax

Step 6 – Apply tax rate to excess

Total growth	£46,120
Less annual allowance	£40,000
Excess	£ 6,120
Apply tax rate – 40%	£2,448*

* Assumes no carry forward allowance available

Example 2 – Includes (Big) Promotion

- Assumptions:
  - 23 years' pensionable service at March 2015
  - Pensionable salary of £110,000 p.a.
  - Receives promotion to £180,000 p.a.
  - CPI 2%
  - Male aged 57

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Calculation of the value of benefits

Step 1 – Start of PIP

- 1 April 2014
- Pay = £110,000
- Service
  - 16 years pre March 2008
  - 6 years post March 2008
- Benefits Payable
- Pension £33,000
- Lump sum £66,000

Step 2 – End of PIP

- 31 March 2015
- Pay = £180,000
- Service
  - 16 years pre March 2008

    6 years post March 2008

    1 year Post March 2014 (CARE)
- Benefits Payable
- Pension £ 57,673
- Lump sum £108,000

Calculation of pension growth

Step 3 – Compare for growth

		Incl. CPI
Pension at start of PIP	£33,000	(£33,660)
Pension at end of PIP	£57,673	
Growth in excess of 2%	£24,013	(A)
Lump sum at start of PIP	£66,000	(£67,320)
Lump sum at end of PIP	£108,000	
Growth in excess of 2%	£40,680	(B)

Calculation of pension growth

Step 4 – Apply factor

Growth in pension	£24,013	(A)
Growth in lump sum	£40,680	(B)
Flat related factor	16	(C)
Growth (A x C) + B =	£424,888	
Excess subject to tax charge	£384,888	

Calculation of tax rate to apply

Step 5 – Calculate marginal tax rate

Gross income	£180,000
Less contributions	£17,580
	£162,420
Plus excess over £40,000	£384,888
Total net income	£547,308

- As all excess is over £150,000 tax charge is 45%

Calculation of tax

Step 6 – Apply tax rate to excess

Total growth	£424,888
Less annual allowance	£40,000
Excess	£384,888
Apply tax rate – 45%	£173,200*

* Assumes no carry forward allowance available

But with carry forward...

Step 4b – Calculate carry forward

- Assuming 2% pay increase and actual inflation in previous 3 years
- Growth total in previous three years
  - £22,949+ £12,295 + £28,227 = £63,471
- Unused allowance
  - (3 x £50,000) - £63,471 = £86,471
- Plus 2015 allowance = £40,000
- Total allowance £126,471

Calculation of tax

Step 6 – Apply tax rate to excess

Total growth	£424,888
Less effective annual allowance	£126,529
Excess	£298,359
Apply tax rate –45%	£134,262

- (Compared to £173,200 if carry forward was not implemented)

Scheme Pays Option

- Charges < £2,000 to be met by member
- Charges > £2,000 Member can elect for scheme to pay whole amount.
- Scheme only obliged to pay if whole charge relates to that scheme

Scheme Pays Option

Step 7 – Calculate pension deduction

Gender	Male
Age	57
Retirement Age	65
GAD CETV Factor	11.93
Tax Charge	£134,262
£134,262/11.93 =	£11,254

Scheme Pays Option

Step 7 – Calculate pension deduction

£134,262/11.93 =	£11,254
Original Pension	£57,673
Less scheme pays deduction	£11,254
Revised pension	£46,419
Pension prior to promotion	£33,000

Other things to consider:

- All pension savings (except State) count towards benefit growth
  - AVCs, added years, additional contributions

- Freedom and Choice
  - If AVCs used as part of new pension freedoms, annual allowance can be reduced to £10,000

Lifetime Allowance

2015 tax regime - summary

- Reduced to £1.25m from April 2014
- LTA valuation factor maintained at 20
- Pension Commutation can reduce tax charges
- Options given to members at retirement
- Includes all pension savings (except state benefit)
- LTA tax-charges - If excess is taken as:
  - Lump sum - taxed at 55%
  - Pension - taxed at 25%

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Calculation of benefits for Lifetime Allowance

- **Pay** **£150,000**
- **Service** **25 years (18 pre 08, 6 post 08, 1 CARE)**
- Pension = (£150,000x18/80)+(£150,000x 6/60) + (£150,000X1/49)
- = £51,811
- Lump Sum = £150,000 x 18 x 3/80
- = £101,250
- Growth = (20 x £51,811) + £101,250 = £1,137,470
- This is <£1,250,000 LTA

From April 2016

- Lifetime allowance reduces to £1.00m from 6 April 2016

Calculation of benefits for Lifetime Allowance

- **Pay** **£140,000**
- **Service** **25 years (18 pre 08, 6 post 08, 1 CARE)**
- Pension = (£140,000 x 18/80)+(£140,000x6/60) + (£140,000 x 1/49)
- = £48,357
- Lump Sum = £140,000 x 18 x 3/80
- = £94,500
- Growth = (20 x £48,357) + £94,500 = £1,061,640
- This is > £1,000,000 (New LTA)

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Protection Racket

HMRC Protections- 2006

- Primary Protection
  - Value of benefits >£1.5m @ 6 April 2006

- Enhanced Protection
  - Value of benefits < or > £1.5m @ 6 April 2006
  - Anyone could apply
  - Some restrictions (including unable to join new arrangement or pay money purchase AVCs)

HMRC Protections 2012

- Life Time Allowance Reduced from £1.8m to £1.5m
- New Fixed Protection Introduced
  - Members retain LTA of £1.8m
  - Strict limits on benefit growth
  - Aimed at members near retirement

HMRC Protections 2014

- LTA reduced to £1.25m
  - 2 New Protections Introduced

- Fixed Protection 2014 (FP2014) (previous fixed protection renamed Fixed Protections 2012 (FP2012)

- Individual Protection (IP)

2014 Protections

- FP2014
  - Retain £1.5m LTA
  - Strict limits on benefits growth
  - Aimed at members near retirement
- IP
  - Value of benefits at least £1.25m @ 5 April 2014
  - Max protection £1.5m
  - No restriction on benefit growth
  - Must apply by 5 April 2017

2016

- LTA planned to reduce to £1m @ 6 April 2016
- New protection(s) expected

Something for the weekend sir?

Not all Protections are reliable!!

- Enhanced and Fixed Protections are lost if a member joins a new “arrangement”
- Does the new Care Scheme count as a new arrangement?
- Could be ok in England & Wales
- Watch for updates

Summer Budget: 8 July 2015

- PIPs to be brought in line with tax year for all schemes
  - 6 April 2016 to 5 April 2017
- Annual allowance to reduce from 6 April 2016
  - Salary over £110,000
  - Pay + pensions growth over £150,000
  - Reduces by £1 for every £2 in excess
  - Pay of £210,000 and above AA reduces to £10,000

Summer Budget Continued

- Special Rules apply in 2015/16
  - 2 PIPs
  - 1 April 2015 to 8 July 2015 (PIP 1)
  - 9 July 2015 to 5 April 2016 (PIP 2)
- Annual Allowance in PIP 1 is £80,000
- Annual Allowance in PIP 2 is Nil
- Unused allowance in PIP1 can be carried forward to PIP2 (maximum £40,000)
- Normal Carry forward rules also apply

Implications for high earners

- Have a second bite at the cherry for 2015/16
- No immediate PIP assessment as at 8 July 2015
- Combined PIP assessment as at 5 April 2016
- AA apportioned across the two PIPS in 2015/16
- CPI for 2015/16 replaced with 2.5%
- Reporting on 2015/16 self assessment tax return

Example

- Assume PIP for combined period (1 April 2015 to 5 April 2016) = £79,566
- PIP 2 = £79,566 x 272/370 = £58,492
- PIP 1 = £79,566 - £58,492 = £21,074

- As PIP 1 < £40,000 can carry forward £40,000 AA to PIP 2
- AA charge on PIP 2 on £18,492 excess over £40,000

New Consultation

- Strengthening the Incentive to save: a consultation on pensions tax relief.
  - 12 weeks
  - Government has “Open Mind”
  - Invites respondents to suggest a better system for providing tax incentives for pension saving
  - Watch for Hymans updates

The Next Steps

- Look for news on the protections
- Seek independent advice before making important decisions.
- Do you or your colleagues need further support?

Consultation on a Public Sector Exit Payment Cap

- The consultation can be found at:
  - https://www.gov.uk/government/consultations/consultation-on-a-public-sector-exit-payment-cap/consultation-on-a-public-sector-exit-payment-cap

- The Hymans 60ss can be viewed at
  - http://www.hymans.co.uk/media/592193/1508-public-sector-exit-payment-cap-bn.pdf

Any questions?

Disclaimer

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