

Pension Tax Relief Changes



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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

£4bn p.a.



80,000

A trip down memory lane

Pre April 2006

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

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Post April 2006

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

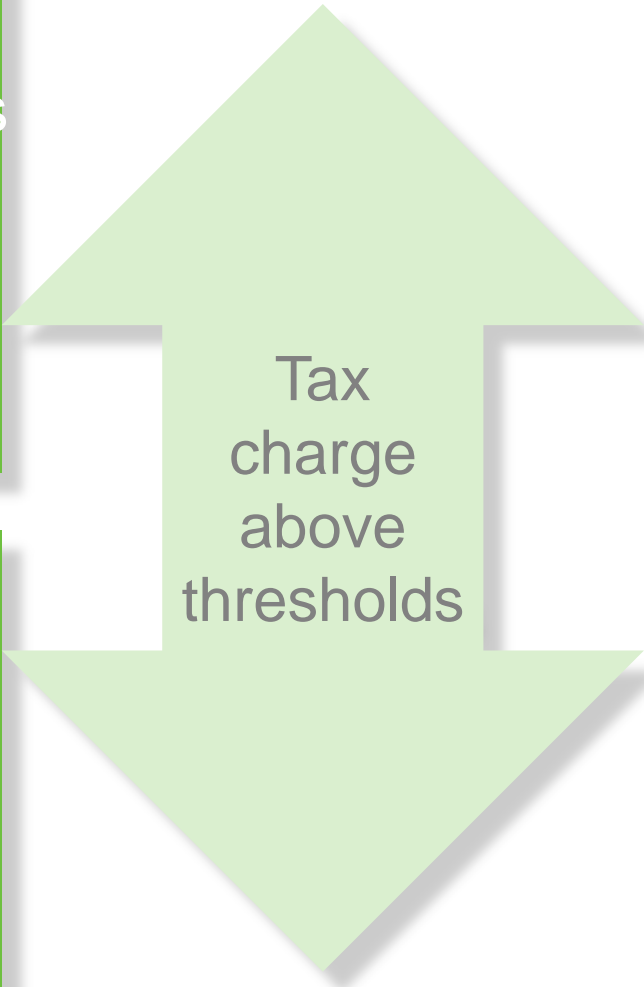
Tax Free Thresholds

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



Tax
charge
above
thresholds

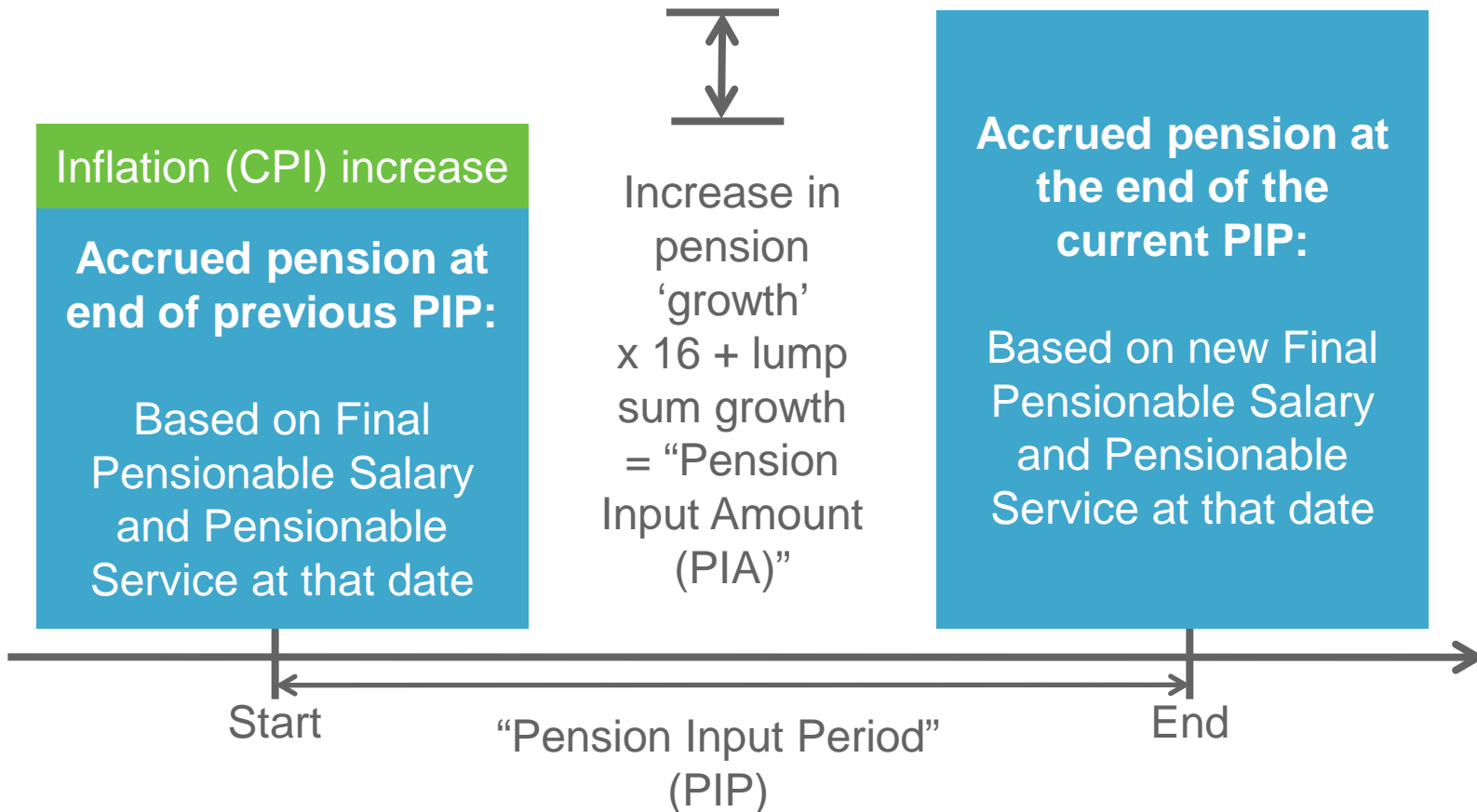


Annual Allowance

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)

PIPs and PIAs



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%



Calculation of the value of benefits

Step 1 – Start of PIP

- 1 April 2014
- Pay = £80,000
- Service
 - 17 years pre March 09
 - 5 years post March 09
- Benefit calculation
 - Pension = $((17 \times £80,000/80) + (5 \times £80,000/60))$
 - Lump sum = $17 \times £80,000 \times 3/80$
- Pension £23,666
- Lump sum £51,000

Step 2 – End of PIP

- 31 March 2015
- Pay £85,000
- Service
 - 17 years pre March 2009
 - 6 years post March 2009
- Benefit calculation
 - Pension = $((17 \times £85,000/80) + (6 \times £85,000/60))$
 - Lump sum = $17 \times £85,000 \times 3/80$
- Pension £26,563
- Lump sum £54,188

Calculation of pension growth

Step 3 – Compare for growth

		Incl. CPI
➤ Pension at start of PIP	£23,660	(£24,140)
➤ Pension at end of PIP	£26,563	
➤ Growth in excess of 2.5%	£ 2,433	(A)
➤ Lump sum at start of PIP	£51,000	(£52,020)
➤ Lump sum at end of PIP	£54,188	
➤ Growth in excess of 2.5%	£ 2,168	(B)

Calculation of pension growth

Step 4 – Apply factor

➤ Growth in pension	£2,433	(A)
➤ Growth in lump sum	£2,168	(B)
➤ Flat related factor	16	(C)
➤ Growth (A x C) + B =	£41,096	
➤ Excess subject to tax charge	£ 1,096	

Calculation of tax rate to apply

Step 5 – Calculate marginal tax rate

➤ Gross income	£85,000
➤ Less contributions	<u>£ 8,535</u>
	£76,465
➤ Plus excess over £40,000	<u>£ 1,096</u>
➤ Total net income	£77,561
➤ As total income is below £150,000 (45% tax threshold) tax charge is 40%	

Calculation of tax

Step 6 – Apply tax rate to excess

➤ Total growth	£41,096
➤ Less annual allowance	<u>£40,000</u>
➤ Excess	£ 1,096
➤ Apply tax rate – 40%	£438*

* 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

Calculation of the value of benefits

Step 1 – Start of PIP

- 1 April 2014
- Pay = £110,000
- Service
 - 17 years pre March 09
 - 5 years post March 09
- Benefit calculation
 - Pension = $((17 \times £110,000/80) + (5 \times £110,000/60))$
 - Lump sum = $17 \times £110,000 \times 3/80$
- Pension £32,542
- Lump sum £70,125

Step 2 – End of PIP

- 31 March 2015
- Pay = £180,000
- Service
 - 17 years pre March 09
 - 6 years post March 09
- Benefit calculation
 - Pension = $((17 \times £180,000/80) + (6 \times £180,000/60))$
 - Lump sum = $17 \times £180,000 \times 3/80$
- Pension £ 56,250
- Lump sum £114,750

Calculation of pension growth

Step 3 – Compare for growth

		Incl. CPI
➤ Pension at start of PIP	£32,542	(£33,193)
➤ Pension at end of PIP	£56,250	
➤ Growth in excess of 2%	£23,057	(A)
➤ Lump sum at start of PIP	£70,125	(£71,528)
➤ Lump sum at end of PIP	£114,750	
➤ Growth in excess of 2%	£43,222	(B)

Calculation of pension growth

Step 4 – Apply factor

➤ Growth in pension	£23,057	(A)
➤ Growth in lump sum	£43,222	(B)
➤ Flat related factor	16	(C)
➤ Growth (A x C) + B =	£412,134	
➤ Excess subject to tax charge	£372,134	

Calculation of tax rate to apply

Step 5 – Calculate marginal tax rate

➤ Gross income	£180,000
➤ Less contributions	<u>£20,410</u>
	£159,590
➤ Plus excess over £40,000	<u>£372,134</u>
➤ Total net income	£531,724
➤ As all excess is over £150,000 tax charge is 45%	

Calculation of tax

Step 6 – Apply tax rate to excess

➤ Total growth	£412,134
➤ Less annual allowance	<u>£40,000</u>
➤ Excess	£372,134
➤ Apply tax rate – 45%	£167,460*

* Assumes no carry forward allowance available

But with carry forward...

Step 4b – Calculate carry forward

- Assuming £2k pay increase and 2% inflation in previous 3 years
- Growth total in previous three years
 - $£27,901 + £28,220 + £28,517 = £84,638$
- Unused allowance
 - $(3 \times £50,000) - £84,638 = £65,362$
- Plus 2015 allowance = £40,000
- Total allowance £105,362

Calculation of tax

Step 6 – Apply tax rate to excess

- | | |
|---|-----------------|
| ➤ Total growth | £412,134 |
| ➤ Less effective annual allowance | <u>£105,362</u> |
| ➤ Excess | £306,772 |
| ➤ Apply tax rate –45% | £138,047 |
| ➤ (Compared to £167,460 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	£138,047
➤ $£138,047/11.93 =$	£11.571

Scheme Pays Option

Step 7 – Calculate pension deduction

➤ £138,047/11.93 =	£11,571
➤ Original Pension	£56,250
➤ Less scheme pays deduction	£11,571
➤ Revised pension	£44,679
Pension prior to promotion	£32,542

Other things to consider:

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

- Freedom of Choice
 - If Avcs used as part of pension liberation, annual allowance can be reduced to £10,000

Annual allowance - who might it affect (LGPS)?

- Pay Award – 4%
- CPI – 2.5%

		Pensionable Salary at start of tax year								
		100,000	110,000	120,000	130,000	140,000	150,000	160,000	170,000	180,000
Pensionable Service at start of tax year	10	31,515	34,666	37,818	40,969	44,120	47,272	50,423	53,575	56,726
	15	33,296	36,625	39,955	43,285	46,614	49,944	53,273	56,603	59,933
	20	35,077	38,585	42,093	45,600	49,108	52,616	56,123	59,631	63,139
	25	36,858	40,544	44,230	47,916	51,602	55,288	58,973	62,659	66,345
	30	38,640	42,504	46,368	50,231	54,095	57,959	61,823	65,687	69,551
	35	40,421	44,463	48,505	52,547	56,589	60,631	64,673	68,715	72,758
	40	42,202	46,422	50,643	54,863	59,083	63,303	67,523	71,744	75,964

Who might it affect (LGPS)?

- Pay Award – 0%
- CPI – 2.5%
-

		Pensionable Salary at start of tax year								
		200,000	210,000	220,000	230,000	240,000	250,000	260,000	270,000	280,000
Pensionable Service at start of tax year	10	40,729	42,766	44,802	46,839	48,875	50,911	52,948	54,984	57,021
	15	34,792	36,531	38,271	40,010	41,750	43,490	45,229	46,969	48,708
	20	28,854	30,297	31,740	33,182	34,625	36,068	37,510	38,953	40,396
	25	22,917	24,063	25,208	26,354	27,500	28,646	29,792	30,938	32,083
	30	16,979	17,828	18,677	19,526	20,375	21,224	22,073	22,922	23,771
	35	11,042	11,594	12,146	12,698	13,250	13,802	14,354	14,906	15,458
	40	5,104	5,359	5,615	5,870	6,125	6,380	6,635	6,891	7,146



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 savings (except state benefit)
- LTA tax-charges - If excess is taken as:
 - Lump sum - taxed at 55%
 - Pension - taxed at 25%

Calculation of benefits for Lifetime Allowance

- Pay £150,000
- Service 25 years (19 pre 09, 6 post 09)

- Pension = $(£150,000 \times 19/80) + (£150,000 \times 6/60)$
- = £50,625
- Lump Sum = $£150,000 \times 19 \times 3/80$
- = £106,875
- Growth = $(20 \times £50,625) + £106,875 = £1,119,375$
- 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 (19 pre 09, 6 post 09)

- Pension = $(£140,000 \times 19/80) + (£140,000 \times 6/60)$

- = £47,250

- Lump Sum = $£140,000 \times 19 \times 3/80$

- = £99,750

- Growth = $(20 \times £47,250) + £99,750 = £1,044,750$

- This is > £1,000,000 (New LTA)

Protection Racket



HMRC Protections- 2006

➤ Primary Protection

- Value of benefits >£1.5M @ 6 April 2006

➤ Enhanced Protection

- Value of benefits < £1.5M @ 6 April 2006
- Anyone could apply
- Some restrictions (including unable to join new arrangement)

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 @ 31 March 2014
- Protection = Value of benefits at 31 March 2014
- Max protection £1.5M
- No restriction on benefit growth
- Must apply by 5 April 2017

2016

- LTA expected to reduce to £1M @ 6 April 2016
- New protection(s) expected
- Budget on 8 July for details

Something for the weekend sir?



Not all Protections are reliable!!

- Enhanced and Fixed Protections are lost if a member joins a new “arrangement”
- New Care Scheme counts as a new arrangement
- Members lose enhanced and Fixed Protection unless they opt out of the CARE scheme.

There may be hope!

- Likely that different rules will apply in E&W
- Maybe some room for negotiation?
- Fingers crossed but watch this space

The Next Steps

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



Any questions?

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