

**The Actuarial Profession**  
making financial sense of the future

Pensions Conference 2012: Fresh perspectives  
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## B4: UK pensions tax relief - the latest

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### Agenda

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- Annual Allowance reduced to £50,000 from tax year 2011/12
- Lifetime Allowance reduced to £1.5m from 6 April 2012
  - Fixed Protection
- Focus on defined benefit.

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## State of play at May 2012

- October 2010 Policy announced
- July/August 2011 Finance Act 2011 given Royal Assent  
Key regulations in force
- March 2011 onward Guidance issued by HMRC  
Sept 2011- Mar 2012 RPSM 700+ pages  
Newsletters, plain English guides
- March 2012 “Snagging” plans announced in Budget  
Fixed Protection, Scheme Pays

– Noting queries raised by ACA [http://www.aca.org.uk/aca-briefing\\_papers.html](http://www.aca.org.uk/aca-briefing_papers.html)

## IMPORTANT JARGON

### Example DB calculation against the 2011/12 AA Active member accruing in a 1/60th scheme

£160,000 x 24/60 = £64,000 pa

+3.1% (CPI 2011/12)

= £65,984 pa

£168,000 x 25/60

= £70,000 pa

£4,016 X 16 = £64,256

£4,016 pa

First £50,000 = No tax

Excess £14,256 taxed at 50% =

**NEW TAX £7,128**

**but check carry forward**

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### but “Valuation assumptions” ... active members and old Inland Revenue limits

- Uncrystallised rights as if reaching “normal pension age”
- March 2012 RPSM pages

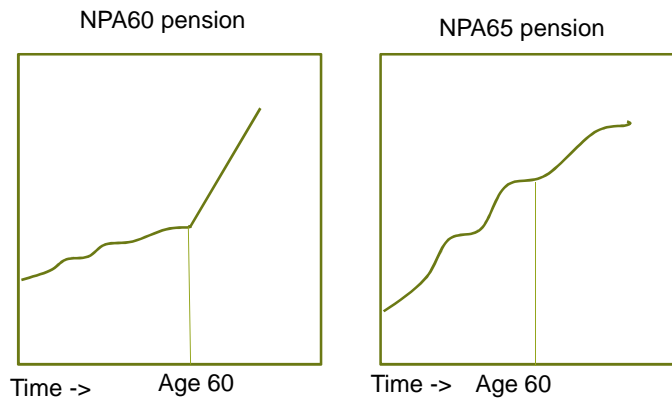
SAMPLE OUTCOME	
Member is accruing benefits (deferred pension measure) at 1/60	PIA (AA used up)
In rules as 1/60	£39,265
In rules as N/NS x 2/3	£15,301
In rules as N/NS x 2/3, with IR limits still in (simple case with no retained benefits)	£78,547

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## but “decisions on DB arrangements” ... active members and split Normal Pension Age

- If scheme provides “late retirement uplift” while in-service, in the scheme rules since before October 2010 HMRC guidance Oct 2011



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## FIXED PROTECTION

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## Lifetime Allowance drop from £1.8m to £1.5m on 6 April 2012

### Fixed Protection (FP)

- While FP holds, a personal £1.8m “underpinned” LTA
  - might be worth £75,000 in saved tax
- Deadline for registration with HMRC was 5 April 2012
  - anyone could register if not then holding Primary or Enhanced Protection
  - 27,000+ applications?
  - HMRC hope: certificates/response by end May 2012
- But FP can be lost.

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## Fixed Protection

### Loss

- When, after 5 April 2012:
  - any Defined Contributions made
    - auto-enrolment
  - on joining a new arrangement (usually)
    - auto-enrolment, life cover
  - on transfer in or out if not “permissible”
    - transactions
  - any Defined Benefit “accrual”
- Member reports promptly if lost – but who monitors in reality?
- Action in one scheme could lose FP for all future tests against the Lifetime Allowance.

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## Fixed Protection

### What is “accrual” in a DB arrangement?

(beware: *broad paraphrasing here*)

An increase in the value of the individual's uncrystallised rights  $(P \times RVF) + LS$

P: annual rate of pension which would, on the valuation assumptions, be payable etc

But ignore increases .. if in no tax year .. they exceed the relevant percentage [for] the tax year.

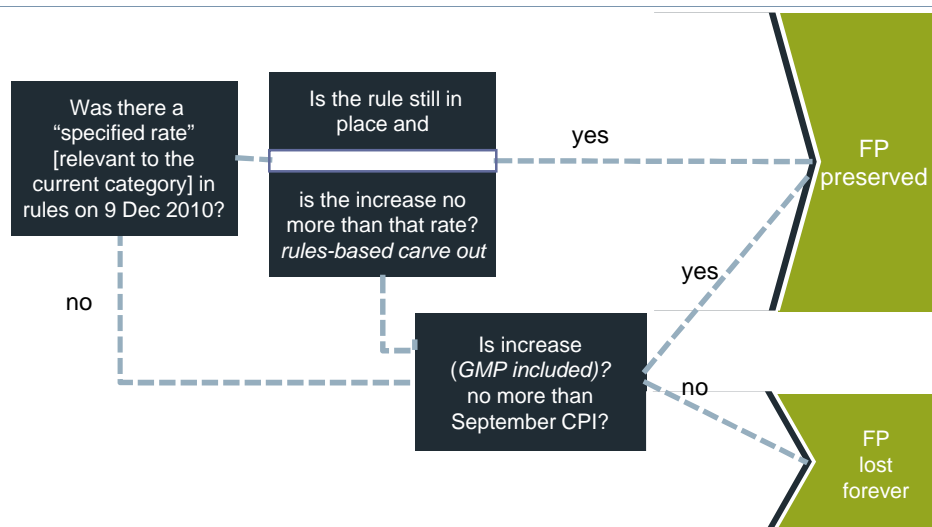
If there is a provision for the rights of the individual to increase during the tax year at an annual rate specified in the rules of the pension scheme on 9 Dec 2010 that percentage..

otherwise,  
CPI  
for September  
in the previous tax year

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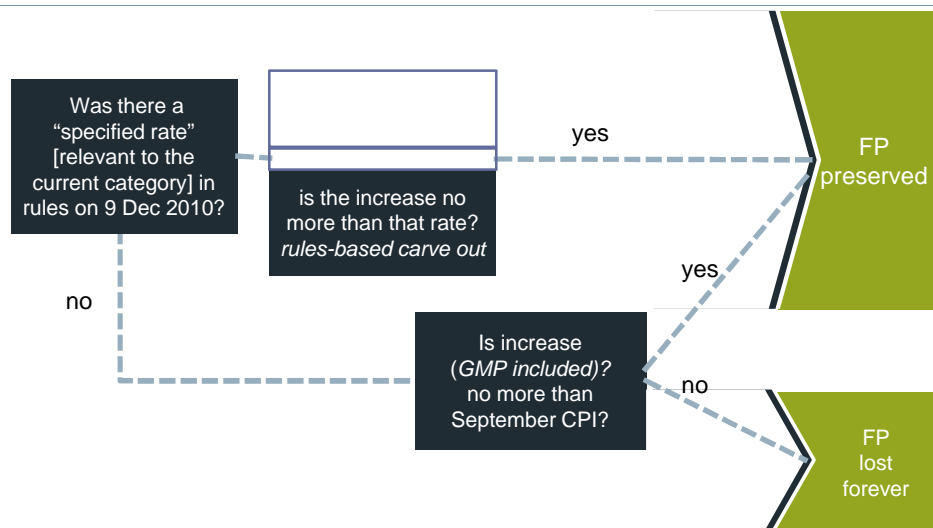
### FP testing of increases in (uncrystallised) benefits: nb per arrangement and each tax year



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## OR?



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## Fixed Protection consulting issues A CURRENT OPPORTUNITY FOR LAW CHANGE

- Focus on deferred pensions?
- What is “specified rate”?
  - discretions
  - by category
  - options exercised at retirement
- What if scheme rule provisions are changed?
  - CPI/RPI issues; buy-ins for RPI; closure-improvements
- If no specified rate, how does the CPI timing issue impact?
- Caps put in so “no benefit accrual that would lose FP”
  - so what is the rules benefit?

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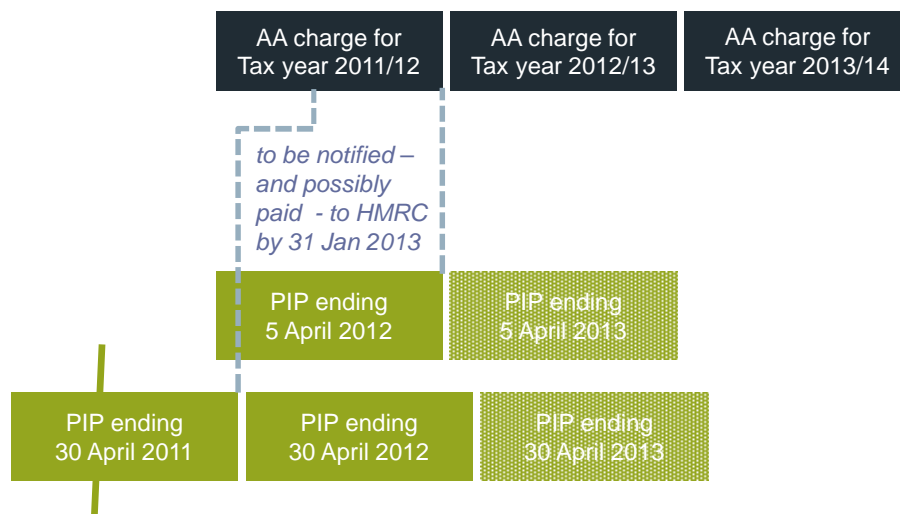
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## ANNUAL ALLOWANCE

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## Annual Allowance - where are members?

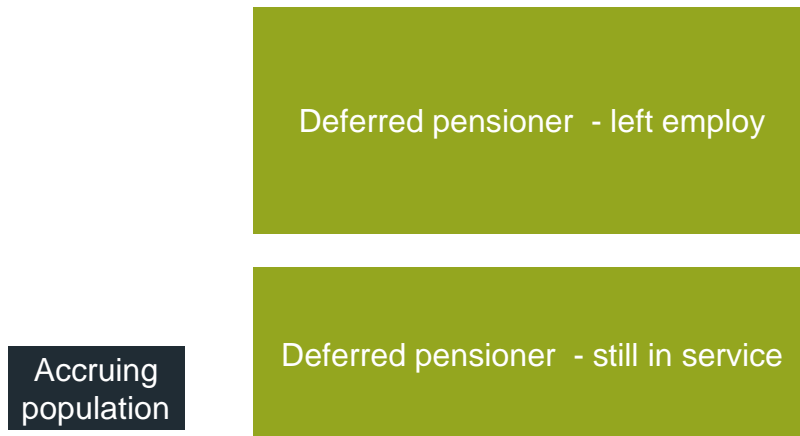


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## Deferred member carve-out for DB arrangements



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## Annual Allowance the deferred member carve out does not apply

### If not a “tax law” deferred member

- No carve-out if “accruing”
  - any salary-linking
  - special [growth?] terms applying until employment ceases
  - in any part of the PIP (so not in PIP of leaving)
  - arrangement structure may be key
  - useful RPSM guidance

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## Deferred members - if carve out from Annual Allowance fails

- Some AA used
- Calculation has potential CPI mismatches
- Potential for charge
- Information obligations
- Creates difficulties in managing future DC
- For “true” deferred members – very unexpected

“Excess” increase on:	£10,000 pa	£30,000 pa	£60,000 pa
+2%	AA use: £3K	£10K	£19K
+5%	£8K	£24K	£48K

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## Annual Allowance deferred member carve-out HMRC AA guidance in March 2012

### A piece of good news

- “Deferred members” of a scheme since before 6 April 2006
- Nil PIA, even if
  - now exercising pre-2006-promised option
  - changed revaluation (if not connected with employment)

### But otherwise similar issues as for Fixed Protection?

- Bulk compared to individual impact?
- And eg at retirement choosing a bridge pension of £7,000 pa from £1,000 whole of life pension creates £96,000 PIA

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## ANNUAL ALLOWANCE AND SCHEME PAYS

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## Annual Allowance and Scheme Pays

### Principle

- Cash flow issue for member
- Member can ask a scheme to pay the AA charge due to HMRC
- in return for a reduction in benefits due from the scheme;
- the member may have a right to do so;
- or not, with the scheme allowing it voluntarily.

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## Annual Allowance and Scheme Pays

### Operation

- Member's **right**, for some of an AA charge for a tax year:
  - the scheme's PIA (AA used up) is £50,000+ and
  - the member's actual AA charge is £2,000+ across all schemes
  - the member makes an election within statutory deadlines
- Scheme Pays changes the effective member overall tax
  - if reduction from benefits due to be taxed (eg pension)
  - and other effects.

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## Scheme Pays - consequential adjustment Issues for the actuary

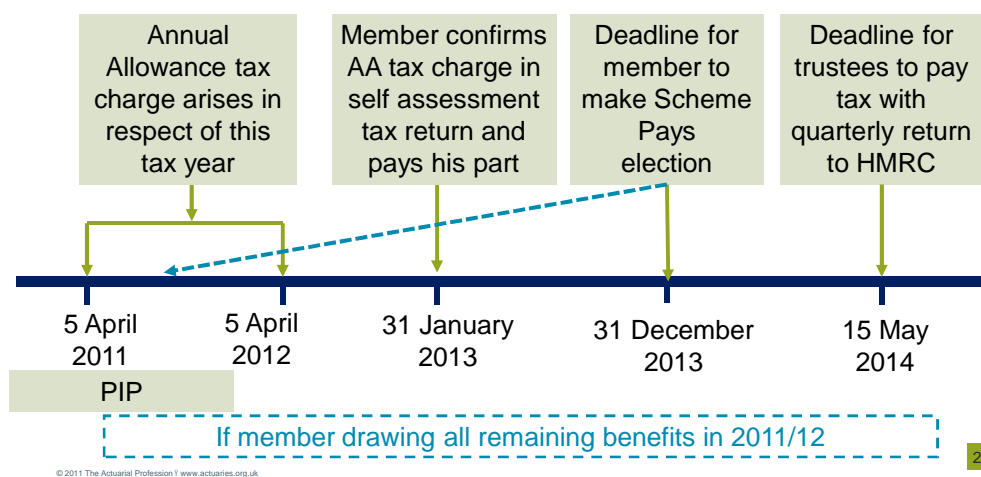
- Set by trustees (if an occupational pension scheme)
  - to the entitlement of the individual to benefits under the scheme
  - just and reasonable having regard to normal actuarial practice
- No charging costs if a tax law right
- HMT policy indicated full flexibility for Trustees of DB schemes.

Use DC Funds	From DB lump sum	From DB pension	Fix now	Defer fixing
			Deferred benefit debit	"Negative DC"
Simplest?	Least tax efficient??	Reduces DB liability	Cash equivalent?	Less admin?

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## Time line for Mandatory Scheme Pays for AA charge arising for 2011/12



## Scheme Pays HMRC guidance March 2012 but see ACA letter

Adjustment constraints	Can be "whole of life" or not Can spread across contingent death benefit or not Cannot be recovered from death lump sum

## Scheme Pays HMRC guidance March 2012 but see ACA letter

Practical issues as a member approaches retirement	
Reduction before tax is paid	No block in principle - but must be after election
Reduction after retirement	Usually "scheme pension must not drop"
Process	Election deadlines don't work
Timing of reduction: tax impact	Tax free cash sum Lifetime Allowance charge <b>Calculation of AA used up</b>
Voluntary Scheme Pays	Some key differences

Member  
elects

Trustees  
apply  
reduction

Trustee  
pays the  
charge

Trustees pay  
the due  
benefit

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## Scheme Pays for an AA charge for the tax year of drawing all entitlement from a scheme

(Adjusted) opening position	FPS x N/60	£20,000	X 16 x 1.052	
Closing position	Nil plus Scheme pension put in place	<del>£25,500</del> <b>£25,000</b>	X 16	
Pension input amount				<del>£71,360</del>
AA plus carry forward, say				£52,000
Excess				<del>£19,360</del>
AA charge				<del>£7,744</del> <b>£4,544</b>

If the AA charge is for a special year  
and the member elects in time to use a right to Scheme Pays  
and the reduction is to DB (lets say -£500 pa for £7,744 tax)  
and the reduction is put in place from the start

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## Scheme retirements now from a scheme three tax years' AA charge may need settling



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## Reminder of the opportunities to change the law:

### On the list

- Fixed Protection
  - “help prevent an individual losing FP in certain specific circumstances”
- Scheme Pays and AA charge
  - Amount, [for] the [tax] year the member takes all their benefits
  - Notice, for the tax year after that of taking benefits
- HMRC thinking now, draft consultation Q04 2012, final Q02 2013
- **What else?**

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## Questions or comments?

Expressions of individual views by members of The Actuarial Profession and its staff are encouraged.

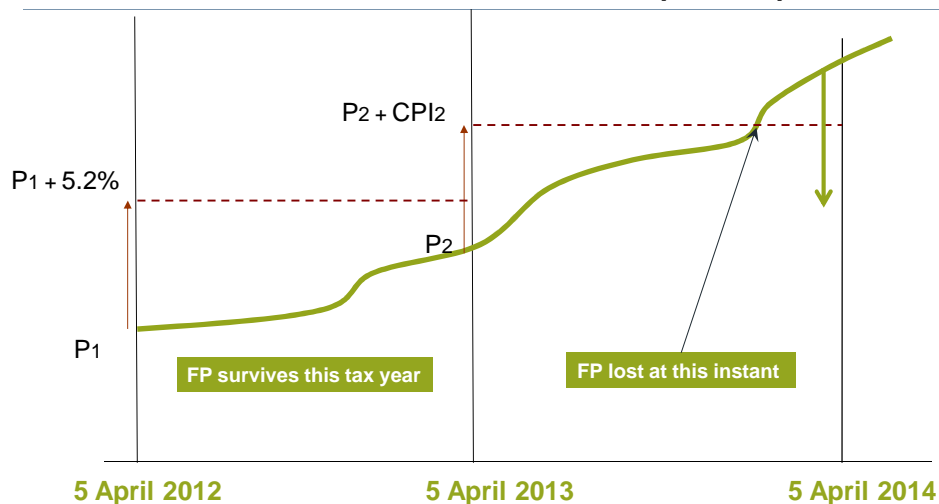
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## A member's undrawn "pension" increases: the test if no rules-based carve out (RBCO)



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## A member's undrawn pension increases, similarly to statutory leaver minimum, but no RBCO

	Days after DOL	Calendar year	N	Relevant revaluation from DOL	"Pension right" for testing benefit accrual	FP "anchor" for next tax year	Tax Year starting the next 6.4	Relevant CPI	FP threshold for the tax year
31/03/2012	0				40,000				
05/04/2012	5	2012	0	0.0%	40,000	40000	2012	5.2%	40,000
06/04/2012	6	2012	0	0.0%	40,000				42,080
31/12/2012	275	2012	0	0.0%	40,000				42,080
01/01/2013	276	2013	0	0.0%	40,000				42,080
31/03/2013	365	2013	1	3.0%	41,200				42,080
05/04/2013	370	2013	1	3.0%	41,200	41200	2013	3.0%	42,080
06/04/2013	371	2013	1	3.0%	41,200				42,436
31/12/2013	640	2013	1	3.0%	41,200				42,436
01/01/2014	641	2014	1	3.5%	41,400				42,436
31/03/2014	730	2014	2	6.6%	42,642				42,436

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## 2011/12 SATR– AA The first tax year in the new AA regime

	"Additional Information" form S101	
8	Amount saved towards your pension, in the period covered by this tax return, in excess of the Annual Allowance	£0.00
9	Annual Allowance tax paid or payable by your pension scheme	£0.00
10	Pension scheme tax reference number	

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