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making financial sense of the future

Pensions conference 2010
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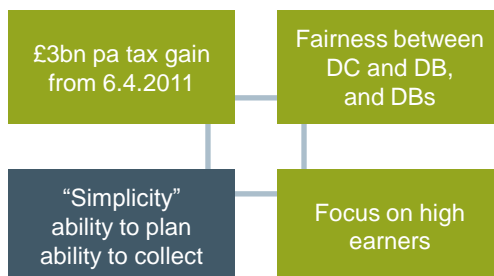
High earner pensions tax Are you ready?

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- This session covers the policy approach set in motion by the Labour government, and is based on the material issued to date by HMT/HMRC and in legislation
- THE BUDGET on 22nd June could announce changes.

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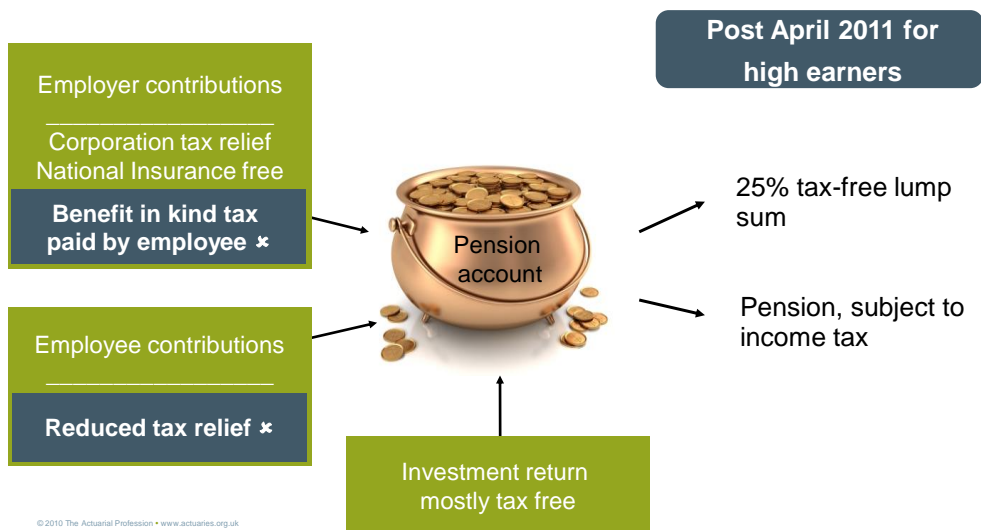
The parameters set for the changes



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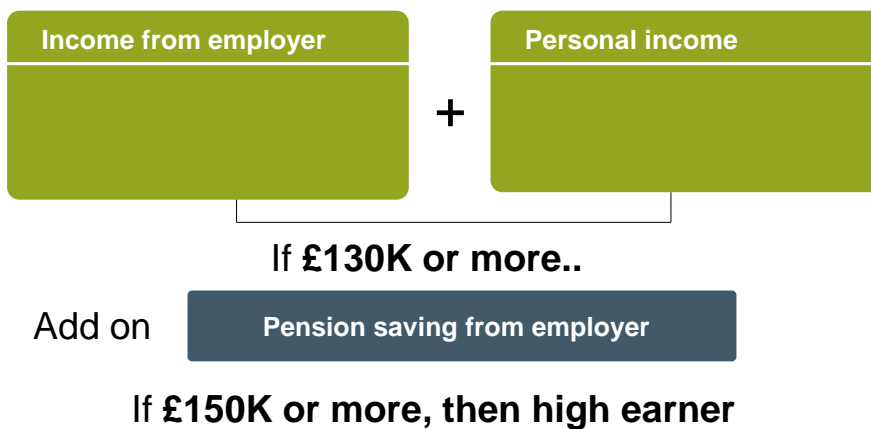
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High earner pensions tax and its interaction with underlying regime



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The annual test for who is “high income”



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Who is affected: HMT numbers

DC	OPS (most SSASs)	135,000	PP	55,000*	190,000
DB	Private sector	50,000	Public sector	60,000	110,000
					300,000

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£130,000 income threshold challenges

- £130,000 to reduce administration
- Huge cliff edge
 - eg salary £120,000 and pension value £50,000
 - add bonus £10,000 = recovery tax £13,000 as well as the £4,200 in income tax and NI
 - “Over self-selection” away from pension
- Salary sacrifice/flex
 - if post 22.4.2009 and for pension: add-back
 - existing employee £140,000, sacrifice for £20,000 pension
 - new recruit £120,000 + £20,000 pension

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KEY FACTS – or “How a regime develops” (1)

- On pension savings made from 6.4.2011
- Income qualifier
- Tax relief restricted to basic rate
- Restriction tapered
 - impact starts at £150,000
 - full impact of restriction to 20% relief at £179,001

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The tax charge

- The taper rate
 - recovery tax between 30 and 0%
 - depends on income plus deemed pension savings paid for by the employer
 - is less if from “40% relieved pay”
- The rate applies to
 - DC contributions
 - Deemed DB value

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Defined benefit – HMT policy specified

- Value
 - Age and NPA Related Factors (ARF)
 - Sparse allowance for quality (pension increases, security)
- Quantum of benefit
 - Leaver measure
 - Inflationary revaluation offset
 - Leaver NPA (in tranches)
 - Enhancements/year of retirement mostly to be recognised

Schemes quantify all this

- Negative values

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Retirement before normal pension age: example D2 in Consultation Document

- Q, **aged 54**, is in a 1/60ths final salary scheme where
- Benefits are payable unreduced from age 55 if retiring from service, or from age 60 if leaving active membership before age 55.
- 10 years' service, pensionable salary of £200,000
5% pay rise to £210,000 (revaluation ignored here for simplicity):
- Pension accrued at 5.4.nn = £33,333 ($=10/60 \times £200,000$);
- Pension accrued to 5.4.nn+1 = £38,500 ($=11/60 \times £210,000$);
- Relevant age related factor is for [age 54/ NPA 60], say 18
- Deemed contribution ($£38,500 - £33,333$) * 18 = **£93,000**.

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Retirement before normal pension age: example D2 ctd

- **A year later**, aged 55, Q receives a pay rise to £220,000 and subsequently retires from active service with unreduced pension.
- Pension accrued to 5.4.nn+2 = £44,000 ($=12/60 \times £220,000$);
- Say ARF for age 55/ NPA 60 = 18.5;
ARF for age 55/ immediate pension is **25**
- Deemed contribution of ($£44,000 \times 25 - £38,500 \times 18.5$) = **£387,800**

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Retirement before normal pension age: round up

- Consultation examples focus on “nil reduction”
- But if HMRC factors differ from the scheme’s?
- Drastic difference between retirements 2010/11 and 2011/12
- Exemptions?
 - Ill health pension enhancement – **probably not**
 - Contributions or enhancements made “*as part of, or resulting from, a redundancy package*” – **no**
 - Year of death or drawing serious ill health lump sum – **yes**
 - “If in-service NPA is different from leaver NPA” - **maybe**

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Negative values

Members of a final salary scheme

For simplicity example highlights only the impact of salary linking on accrued benefits



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KEY FACTS – or “How a regime develops” (2)

- Member to manage the tax
 - through Self Assessment Tax Return
 - employer/scheme to identify many and provide information
- Tax upfront
 - for large bills: “Scheme Pays”

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Finance Act 2010

- Covers high income test and charge rates
- Framework for DB valuations
- Anti-avoidance

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What is outstanding – HMT’s list 24th March 2010 particularly relevant for DB

- Age-related factors
 - basis, actual numbers, manner of operation
 - year of retirement/enhancement?
- Credits for years when DB values drop in real terms
- “Scheme Pays” term for benefit deduction
 - design, calculation, grossing-up

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What is outstanding – HMT’s list 24th March 2010 other

Income test

- Taxable redundancy
- For tests in the year of drawing benefit look at current and previous year: details

Administration

- Scheme Pays if multiple schemes / when it need not be offered
- The employer/scheme information process

Overseas schemes

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Alternative vehicles Budget April 2010 announcement

“The Government also announces future action to tackle the use of arrangements to reward employees through the use of trusts or other intermediaries, with the purpose of avoiding, deferring or reducing liabilities to income tax and NICs or avoiding restrictions on pensions tax relief. The Government will consider options for tackling these avoidance arrangements with the intention of introducing any necessary legislation to take effect from April 2011.”

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Anti-avoidance - Finance Act 2010

Section 213 O (not verbatim)

A “scheme” is caught if all three of:

- A:** Reasonable to assume main purpose avoiding the new tax
- B:** [Relevant] income or pensions savings in a tax year reduced
- C:** Reduction(s) redressed by
 - increasing [relevant] income/pensions savings in another tax year or
 - “The provision at any time of some other benefit to or for the benefit of the individual or any person who is a dependant of, or is connected with, the individual”

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Questions or comments?

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