The Actuarial Profession
making financial sense of the future

Pensions Conference 2012: Fresh perspectives: re-presented 19 November 2012
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UK pensions tax relief - the latest

Agenda

- Annual Allowance reduced to £50,000 from tax year 2011/12
- Lifetime Allowance reduced to £1.5m from 6 April 2012, with Fixed Protection option
- Defined benefit focus

- Known unknowns – active members
- Lobby points – deferred members
- Scheme Pays

State of play at 15 November 2012

• October 2010	Policy announced
• July/August 2011	Finance Act 2011 given Royal Assent Key regulations in force
• March 2011 onward Sept 2011- Mar 2012	Guidance issued by HMRC RPSM 700+ pages Newsletters, plain English guides
• March 2012	“Snagging” plans announced in Budget draft regulations in the Autumn
• 5 December 2012	Autumn Statement

And queries raised by ACA http://www.aca.org.uk/aca_briefing_papers.html

TECHNICALITIES THAT HAVE TURNED OUT TO BE IMPORTANT

Example DB Annual Allowance
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

“Finance Act 2004 Valuation assumptions”

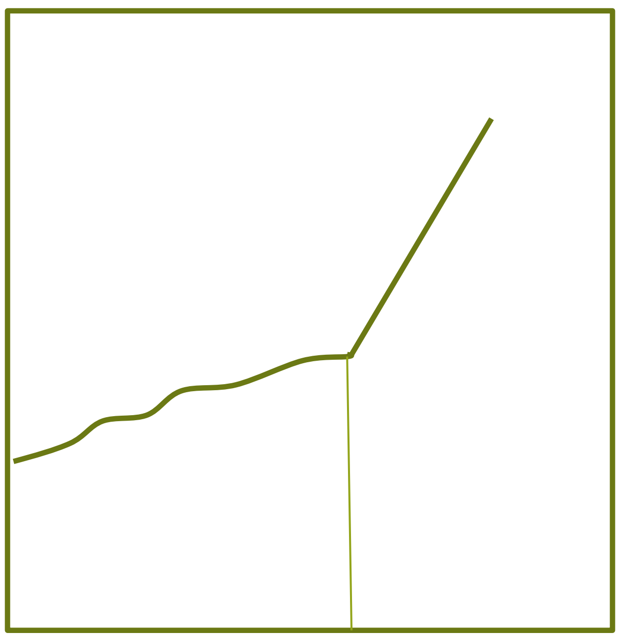
- Assess rights as if at “normal pension age”
- March 2012 RPSM: active members with “Inland Revenue” limits

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

DB *arrangements* decisions
Active members and split Normal Pension Age

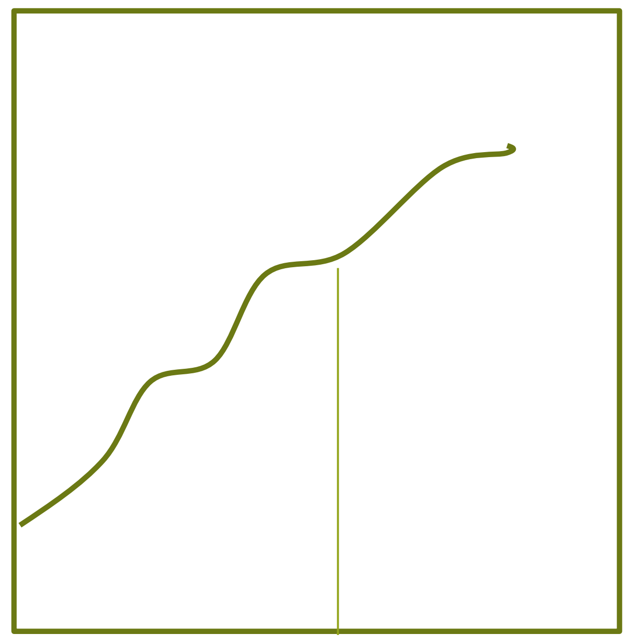
- If scheme provides “late retirement uplift” while in-service, in the scheme rules since before October 2010 HMRC guidance Oct 2011

NPA60 pension



Time -> Age 60

NPA65 pension



Time -> Age 60

Issues for deferred members

Deferred pensioner - left employ

Accruing population

Deferred pensioner - still with the employer

Fixed Protection why do employers/trustees have to worry?

- Lifetime Allowance drop from £1.8m to £1.5m on 6 April 2012;
- Fixed Protection gives a personal £1.8m “underpinned” LTA;
  - might be worth £75,000 in saved tax;

- By the deadline of 5 April 2012: 27,000 registrations;

- Fixed Protection can be lost;
- And action in one scheme could lose FP for all future tests against the Lifetime Allowance.

Annual Allowance “deferred member carve-out” why do employers/trustees have to worry?

If the carve out does not apply

- Some Annual Allowance used;
- Complex unexpected calculations
- Potential for charge
- Information obligations
- Creates difficulties in managing future DC
- Member very surprised

Fixed Protection

How can it be lost?

- When, after 5 April 2012:
  - Defined Contributions made
  - joining a new arrangement (usually)
  - transfer in or out if not “permissible”
    - auto-enrolment, life cover, transactions
  - any Defined Benefit “accrual”

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 x 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

Fixed Protection consulting issues (with Annual Allowance DMCO parallels)

- What is “specified rate”?
  - by category?
  - discretions
  - options exercised at retirement
- What if scheme rule provisions are changed?
  - closure-improvements; CPI/RPI issues; buy-ins for RPI
- If no specified rate, what is the CPI calculation?
  - versus statutory-style leaver revaluation
  - as per technical appendix?
- GMPs
- Safe if cap put in of “no benefit accrual that would lose FP”?

SOME FURTHER POINTS ON ANNUAL ALLOWANCE

Annual Allowance “deferred member carve-out” and employees

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)
  - RPSM guidance is key

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

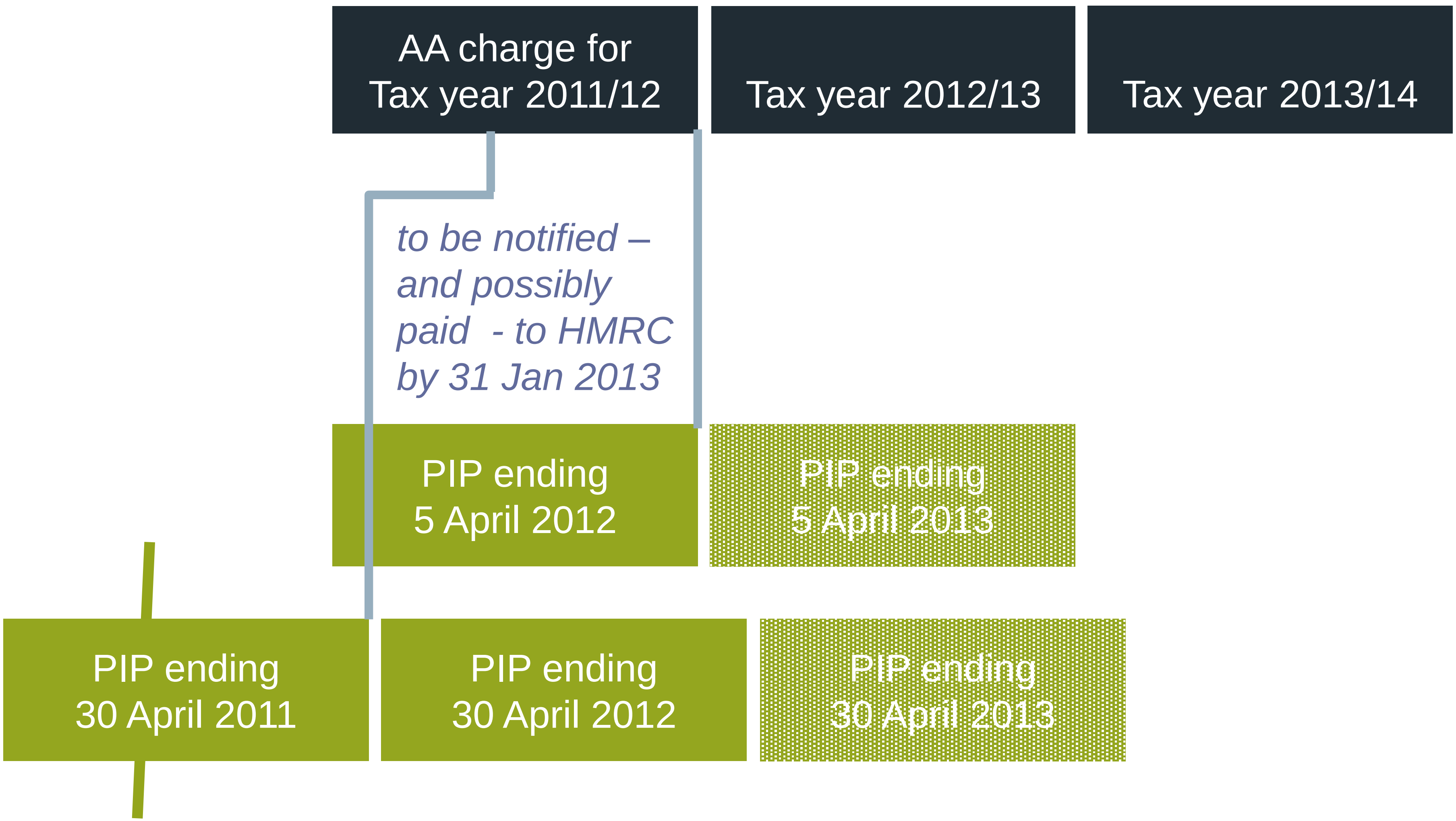
Similar issues as for Fixed Protection

- eg a retirer converting £1,000 pa whole of life pension for a bridge of £7,000 pa uses £96,000 of AA

A piece of good news

- "Deferred members" of a scheme since before 6 April 2006
- Do not use up AA, even if
  - now exercising pre-2006-promised option
  - changed revaluation (if not connected with employment)

Annual Allowance - where are members?



2011/12 tax return
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	

ANNUAL ALLOWANCE AND SCHEME PAYS

Annual Allowance and Scheme Pays

Principle

- Cash flow
- Member can ask a scheme to pay the AA charge due to HMRC
- in return for a reduction in benefits due from the scheme;
- as if right;
- or not, with the scheme allowing it voluntarily.

Annual Allowance and Scheme Pays

Operation

- Member's **right**, for some AA charge for a tax year:
  - the scheme's PIA (AA used up) is £50,000+ and
  - the member's actual total AA charge is £2,000+
  - the member makes an election within statutory deadlines

- Using Scheme Pays changes the member's overall tax
  - if reduction from benefits due to be taxed (eg pension)
  - and other effects.

Scheme Pays - consequential adjustment
Issues for the actuary

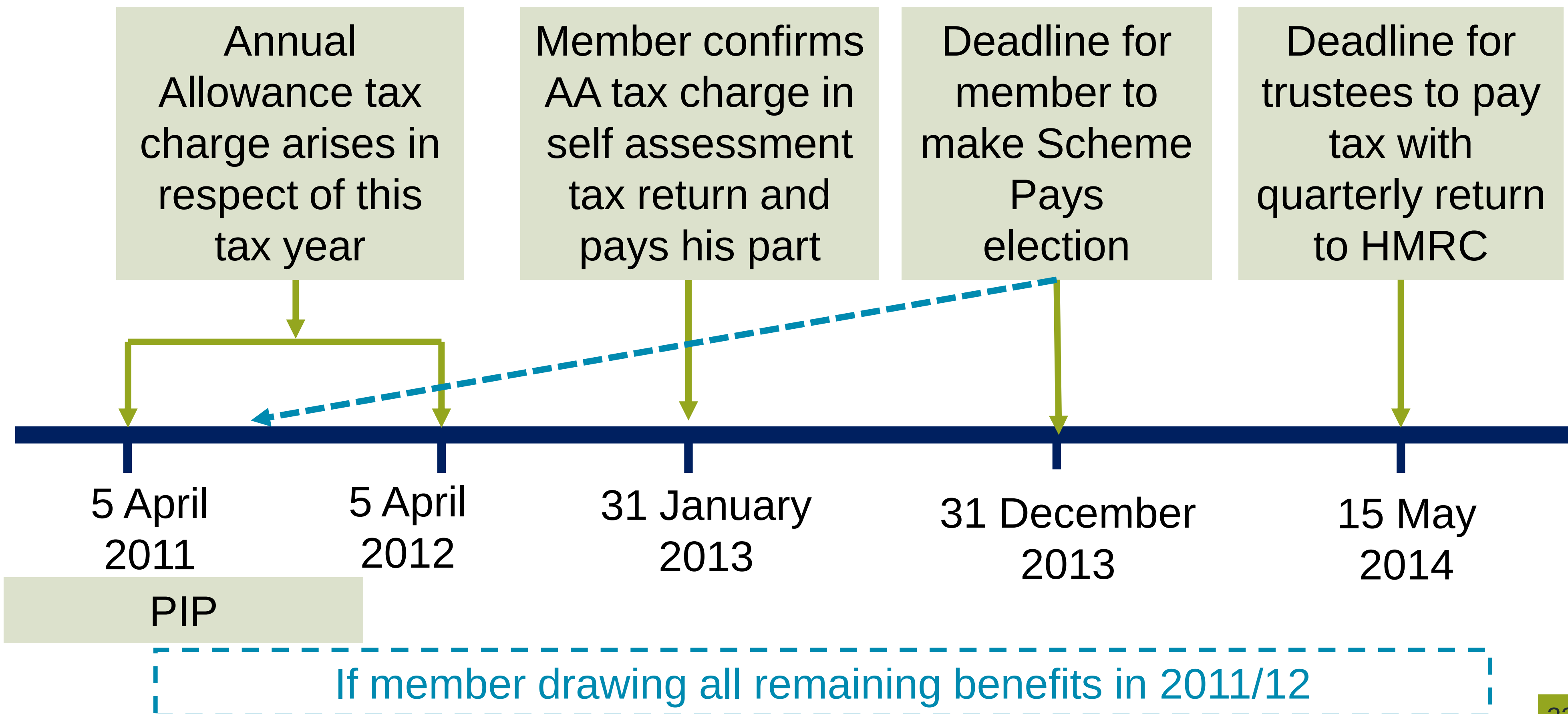
- Set by trustees (if an occupational pension scheme)
  - to the entitlement of the individual to benefits under the scheme
  - just and reasonable having regard to normal actuarial practice
- No charging costs if a tax law right
- HMT policy indicated full flexibility for Trustees of DB schemes.

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?

Scheme Pays
HMRC guidance March 2012

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

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



Scheme Pays practicalities
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
Timing of reduction: tax impact	Tax free cash sum Lifetime Allowance charge Calculation of AA used up
Voluntary Scheme Pays	Some key differences

Member elects

Trustees apply reduction

Trustee pays the charge

Trustees pay the due benefit

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	~~£25,500~~ £25,000	X 16	
Pension input amount				~~£71,360~~
AA plus carry forward, say				£52,000
Excess				~~£19,360~~
AA charge				~~£7,744~~ £4,544

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

Changes we are anticipating in the draft legislation with limited consultation window

- AA deferred member carve out (DMCO)
  - RPI-restoration; CPI/RPI deferred annuity contracts; statutory-type revaluation;
- DB to DB transfers for mirror image benefits;
- Scheme Pays AA charge anomaly;
- Scheme Pays election deadlines.

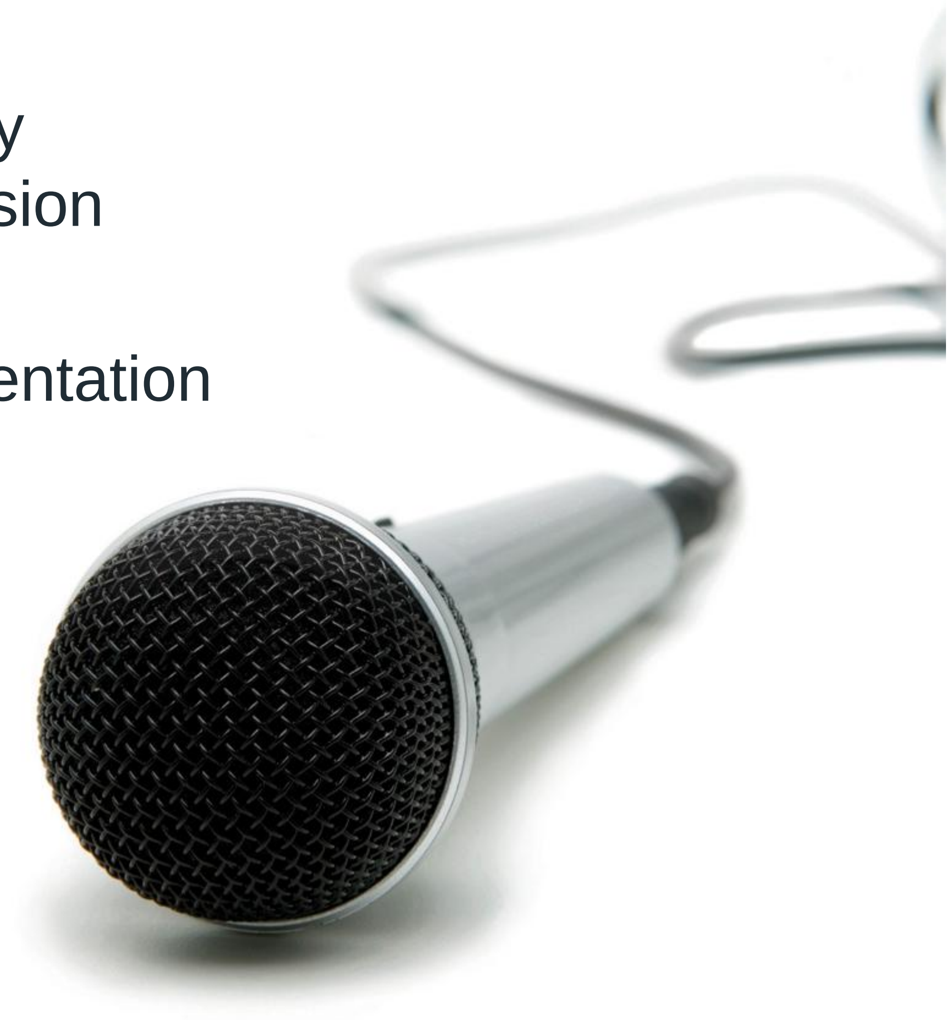
And in later release?

- FP not lost if “no fault of member” - similar to DMCO above;
- Scheme Pays post-retirement reductions to pension eased;
- Bridges ceasing after age 65 to be authorised.

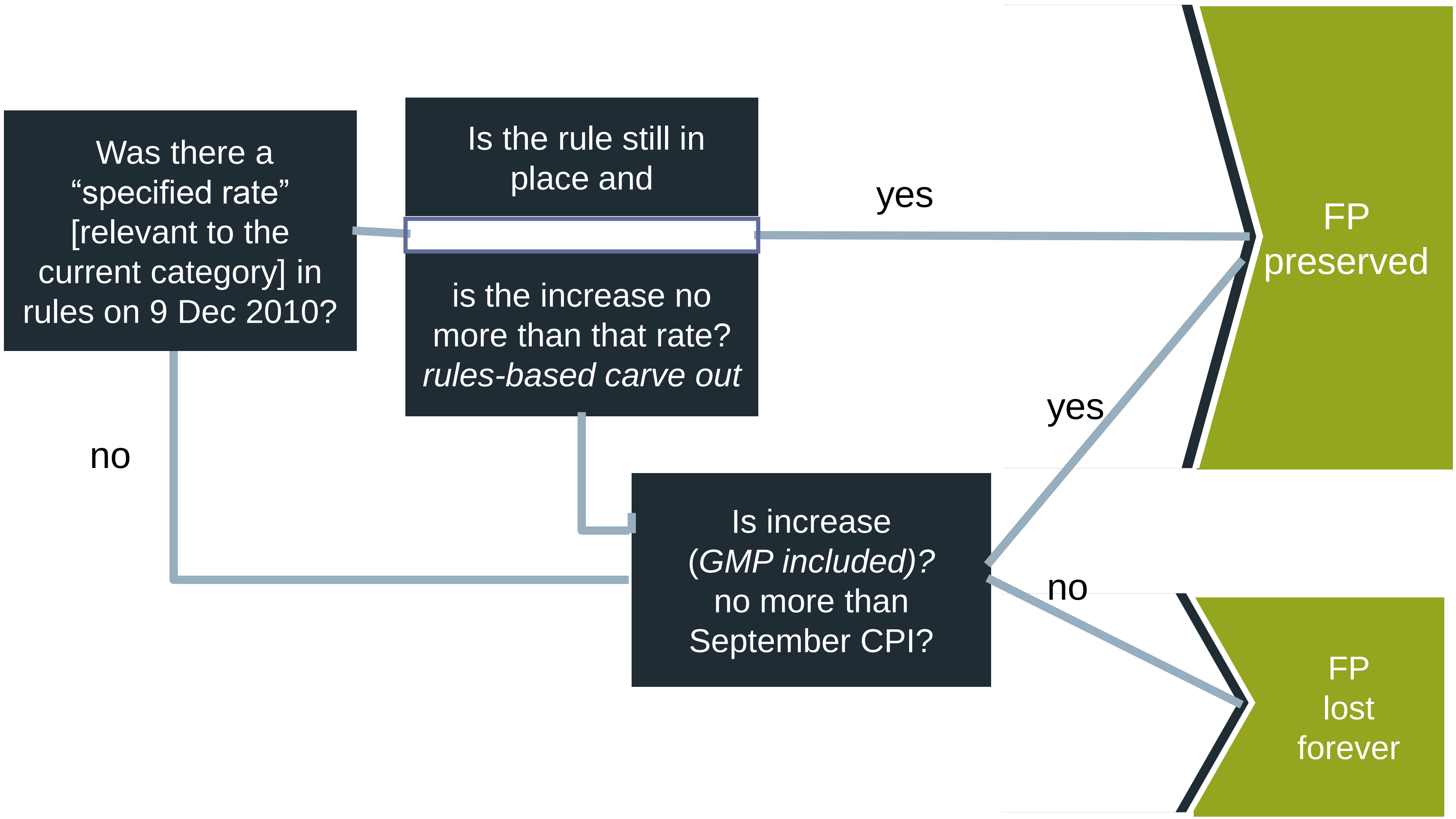
Questions or comments?

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

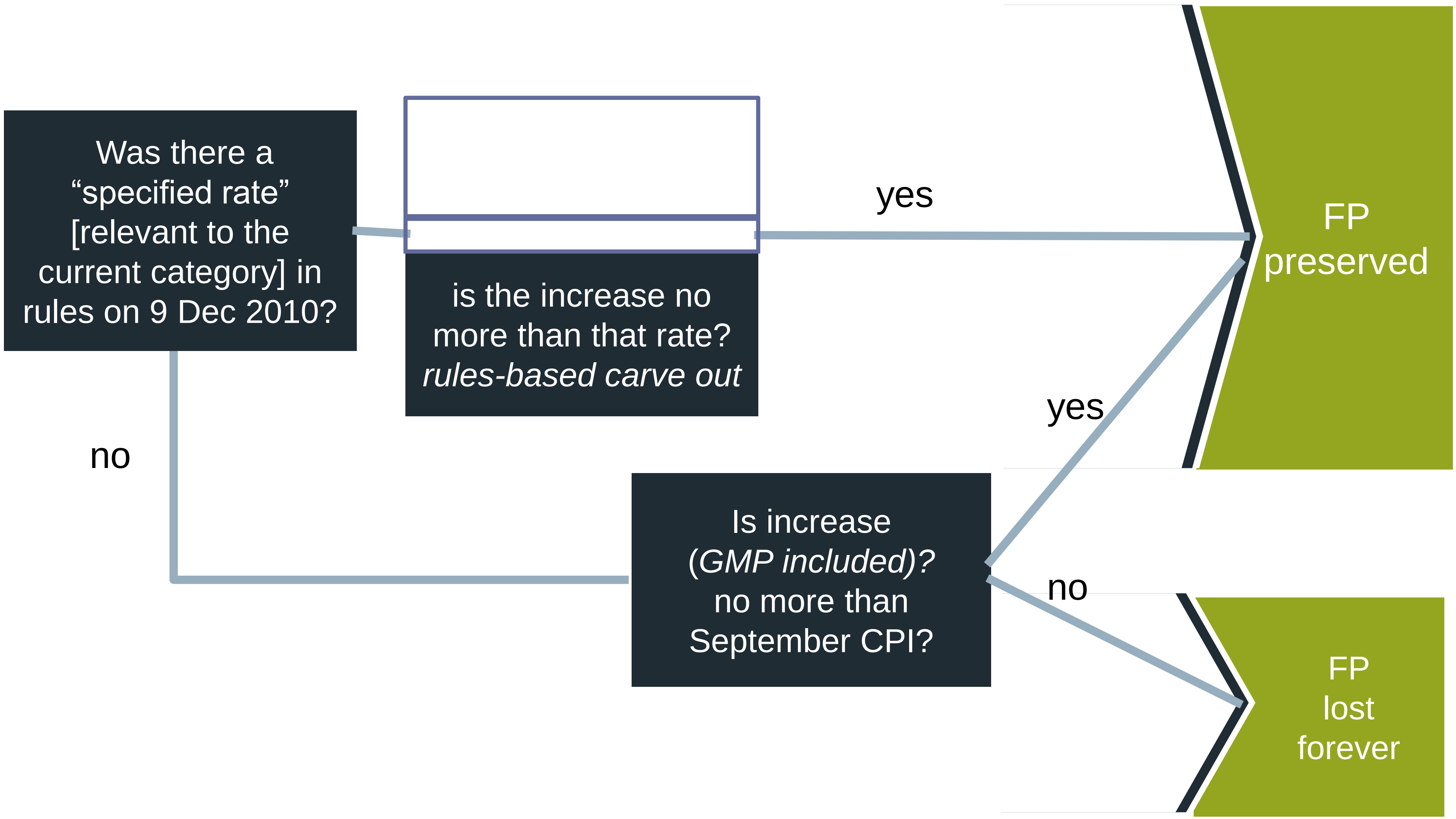
The views expressed in this presentation are those of the presenter.



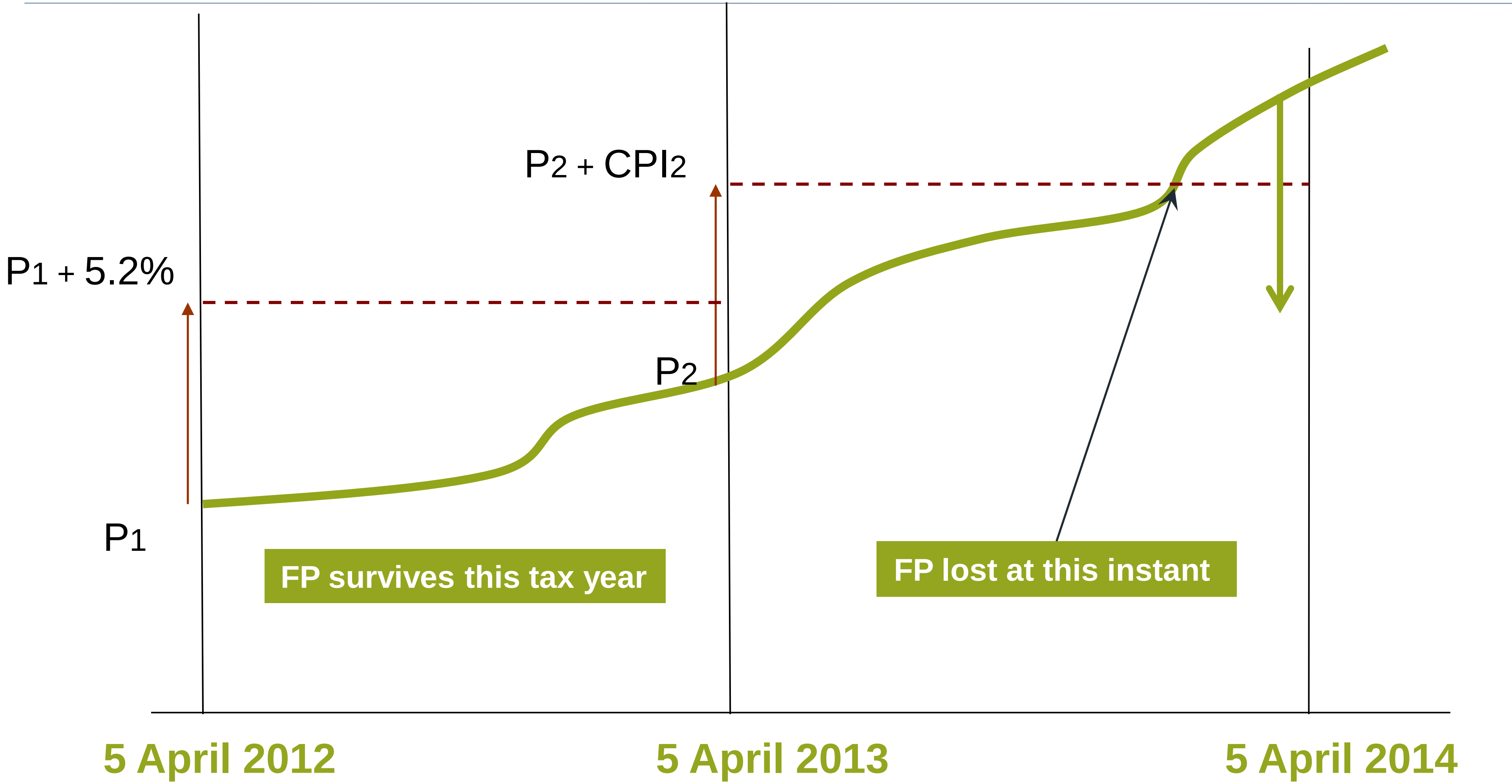
FP testing of increases in (uncrystallised) benefits: nb per arrangement and each tax year – maybe (1)



FP testing of increases in (uncrystallised) benefits: nb per arrangement and each tax year – maybe (2)



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



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

November 2012 draft regulations relating to Annual Allowance Deferred Member Carve Out

Includes

- For the purposes of subsection (5AA)
- there is to be taken to have been no increase in the value of the relevant rights of the [deferred member] during the PIP where
- the whole of what would otherwise be such an increase is the result of any provision contained in or made under an enactment.