AEGON | Trustee Solutions

For trustees

DB Matters – tax relief bulletin

June 2011

You might recall that in December last year, we told you about the government's announcement on the new allowances for tax-relieved pension saving. We said that we'd write to you again with more detail and examples as soon as the full extent of the changes became clear.

To recap, the headline changes were:

1. The annual allowance (AA) would be reduced from £255,000 to £50,000 from April 2011.
2. The lifetime allowance (LTA) would fall from £1.8 million to £1.5 million from April 2012.
3. The valuation factor used to calculate the value of defined benefits pension savings was to increase from '10' to '16' from April 2011.

More detailed information will follow on the implications of lifetime allowance nearer April 2012, and the new valuation factors were covered in some detail in our December newsletter.

However, the government has recently announced a number of measures relating to the reduction in annual allowance that we'd like to give you more detail on.

This bulletin is simply intended to give you an overview of the changes. If you need more detailed information specific to your scheme, you should speak to a financial adviser.

Pension input periods – is there any action needed?

The reduction in the AA means that the pension input period (PIP) – the period during which a member's pension savings in an arrangement are measured for the purpose of testing against the AA for the tax year in which that PIP ends – may have become relevant to many more of your members than before.

Key facts in the application of the new AA to PIPs

- If a PIP ended in the 2010/2011 tax year, the previous AA of £255,000 will apply to pension saving during that PIP.
- If a PIP ends in the 2011/2012 tax year and began or will begin after 14 October 2010, the new AA of £50,000 will apply to all pension saving during that PIP.
- If a PIP ends in the 2011/2012 tax year and began before 14 October 2010, under the transitional provisions in the Finance Bill 2011, the previous AA of £255,000 will apply to pension savings made over the whole of that PIP, but any pension saving after 14 October 2010 until the end of the PIP will be subject to the £50,000 limit.

Nominating a new end date for a PIP ending in the 2011/2012 tax year

A particular problem arises in relation to defined benefit schemes which were in existence on 5 April 2006. Unless the PIP has been defined (for example, by adopting a new set of scheme rules that define the PIP, by including it in a deed of amendment or just by means of an announcement to members) the default PIP will run from 7 April 2010 to 6 April 2011. The new AA will therefore apply to any pension saving made after 14 October 2010.

To enable members to make use of the higher AA for as long as possible, you may wish to nominate a new end date for your current PIP (if you haven't done so already) to bring the end date into the 2010/11 tax year. There can only be one PIP ending in each tax year and a PIP can't be longer than 12 months, so the only way that you can bring the end date of the PIP within the 2010/11 tax year is to make a retrospective nomination back to A-Day (6 April 2006).

In other words, you'll need to change the end date of the first PIP to a date falling on or before 5 April 2007. This would allow for all subsequent PIPs to end on the same date each year. The PIP need not be aligned with the tax year - in other words, you may find it more convenient for the PIP to coincide with the scheme year.

Act now?

The ability to make retrospective nominations looks set to disappear when the Finance Bill 2011 receives Royal Assent. This may be as soon as 1 July, so if you want to make this change, time is running out. Be aware that changing a PIP could affect a member's tax liability as a result of pension saving falling within a different tax year.

Annual allowance charges

The responsibility for working out if an AA charge is due falls directly on a member. The Scheme Administrator is legally required to issue a statement to each member whose pension input amount (PIA) or pension savings under that scheme during a given PIP exceeds the AA for the relevant tax year.

A member can ask the Scheme Administrator to confirm the pension savings made for them for a particular PIP, and the Scheme Administrator must comply with this request.

A 'mandatory' statement for a member with a PIA greater than the AA must be issued no later than 6 October following the end of the relevant tax year, except where the tax year is 2011/2012 – in this case, the Scheme Administrator must provide the member with the statement no later than 6 October 2013. When the member requests the statement it must be provided within three months of that request, or by 6 October following the relevant tax year, if later.

Meeting tax charges from pension benefits (scheme pays)

Where a member exceeds the AA in a particular scheme and their liability to the AA charge is greater than £2,000, they can elect for the pension scheme to pay the charge in full.

If a member chooses this option, the scheme must pay the tax charge, unless the scheme enters a Pension Protection Fund assessment period or can demonstrate to HM Revenue & Customs that paying the charge would be to the substantial detriment of the interests of scheme members. The charge is to be paid when it arises. Schemes cannot charge members for exercising the 'scheme pays' option but can reduce the member's benefits.

Reduction of benefits

Where a scheme pays the tax charge on a member's behalf, the member's entitlement to benefits must be adjusted on a 'just and reasonable' basis 'having regard to normal actuarial practice'. The Treasury has indicated that it wishes to provide schemes with flexibility as to how the reduction in the member's benefit should be applied in order to fund the tax change – and the summary of responses document indicates a number of possible options.

Carry-forward of any unused annual allowance

Subject to certain conditions, any unused AA can be carried forward for up to three years.

Unused AA can only:

- arise in a year where the individual was a member (active or deferred) of a registered pension scheme
- be used in a year where that year's full AA has been used

The amount that can be carried forward to a current tax year is:

- any excess allowance (ignoring any carry-forward amount) for the tax year immediately preceding the current tax year, plus
- any excess allowance (ignoring any carry-forward amount) for either or both of the two tax years immediately preceding the tax year before the current tax year that has not been 'used up'

Excess allowance is used up if:

- for any tax year between that tax year and the current tax year, the total pension input amount was more than the annual allowance, and
- the excess AA was used to reduce or eliminate the AA charge for that intervening year

Where the member has unused allowance in more than one of the previous three years, the earliest year's unused allowance would be used up first.

The carry-forward provisions apply automatically (in other words, the member doesn't have to apply for the increased allowance). It applies as if the AA limit for the tax years 2008/09, 2009/10 and 2010/11 was £50,000.

Calculations to determine if there is any excess AA for those years should be made on the new basis (applying from 6 April 2011). From 6 April 2011, it will be possible to carry forward unused AA from the previous three tax years. This can only be done if a member uses up the full AA in the tax year they want to use carry forward in.

Feedback

Have you found this bulletin useful? Are there any subjects you'd like us to include in future bulletins? Let us know what you think. Please email your comments to atsmb@aegon.co.uk

The information in this newsletter is based on our understanding of current and proposed law, and HM Revenue & Customs practice, which may change.

The table below shows an example of how any unused annual allowance might be carried forward.

Tax year	2008/09	2009/10	2010/11
National annual allowance	£50,000	£50,000	£50,000
Pension input amount	£40,000	£70,000	£20,000
Carried forward annual allowance	£50,000 - £40,000 = £10,000	£50,000 - £70,000 = minus £20,000 plus £10,000 = minus £10,000 (as this is negative use zero)	£50,000 - £20,000 = £30,000 plus zero = £30,000
Total available to carry forward	£10,000	Zero	£30,000

I hope that you've found the information in this bulletin helpful. If you have any questions, please get in touch with your usual AEGON Trustee Solutions contact or speak to your financial adviser.

Dougie Burton
Head of Specialist Services

AEGON | Trustee Solutions

AEGON Trustee Solutions is a brand name of Scottish Equitable plc, Guardian Assurance plc and Guardian Pensions Management Ltd. All are authorised and regulated by the Financial Services Authority. Scottish Equitable plc, registered office: Edinburgh Park, Edinburgh EH12 9SE. Registered in Scotland (no. 144517). Guardian Assurance plc and Guardian Pensions Management Ltd, registered office: Ballam Road, Lytham St Annes, Lancashire, FY8 4JZ. Registered in England (nos. 38921 and 985480). All are AEGON companies. www.aegontrusteesolutions.co.uk

C 276881 ATS 00266935 05/11