

# Talking points – Pension changes, Budget 2009

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Although many commentators had predicted that the Chancellor might have higher rate tax relief on pension contributions within his sights, not many expected him to make proposals that are so far reaching or complicated.

In this Talking Points we look at some of the issues arising from the proposed changes

## The changes from 2011

The government has announced its intention to restrict tax relief on pension contributions, including those made by employers, for individuals with an annual income of £150,000 or more. The tax relief will be tapered from full relief to 20% (the basic rate level) for those earning over £180,000. HMRC will consult on the implementation of these new rules.

## What is the impact now?

In order to prevent individuals from paying large contributions before the new rules apply, HMRC has introduced “Anti-forestalling measures”. These measures affect those individuals:

- » whose earnings are in excess of £150,000 in this tax year or either of the previous two tax years; and
- » who change their normal regular ongoing pension savings (as defined in the draft legislation - it should be noted that this only includes contributions that are made quarterly or more frequently); and
- » whose total gross pension contributions following any change to their normal regular ongoing pension contributions, including employer contributions, exceed £20,000.

The tax charge proposed is currently 20% on the excess over either:

- » £20,000 if their pension savings were previously below £20,000; or
- » the difference between their normal regular pension contributions and the new level of contributions.

One exception to this is defined benefit scheme members where whatever the level of their earnings the protected input amount will include the whole of their Defined Benefit scheme irrespective of any increases in accrual. This applies also to new joiners, provided the scheme has 50 or more members.

## Earnings

The definition of relevant income for the purpose of anti-forestalling is not the same as that previously understood for net relevant earnings. The biggest change is the inclusion of dividend income in the calculation. This will result in many of those who have previously been paid mainly in dividends but contributed ad hoc to their pensions through employer contributions being caught by these new rules.

In addition, those individuals entering into salary sacrifice arrangements on or after 22 April 2009 will have to include the value of the sacrificed income in the calculation of relevant income. This does not affect those with arrangements made prior to 22 April, however it is unclear if arrangements entered into but not commenced will be classed as regular contributions.

## Our view

The interim rules are unnecessarily complex, evidenced by the 52 page technical guide produced by HMRC to try and explain the rules, and may catch out those who were intent on saving for their retirement rather than simply reducing their tax bill.

It is unfortunate that those who paid contributions on the 22 April are inadvertently affected by these rules, along with those with earnings over £150,000 in the last couple of tax years whose earnings have now fallen given the credit crunch. In addition, those who deferred contributing to pensions, by virtue of the A-day rules, until later in their careers will be hard hit, but those who chose to fund their pensions early will be much less affected.

It is self-employed individuals who are most likely to suffer under the new rules, because they tend to have more erratic earnings than employed individuals and are less able to plan their contributions over the longer term.

We are of the view that in the short term this will not have a massive impact on the SIPP market as many SIPPs are funded in part or in total by transfer values from other schemes. Longer term it must have a negative impact on the quantum of pension savings by "high earners" which will in turn affect the size of transfer values and possibly reduce the attractiveness of switching to a SIPP - although of course there are many reasons why investors like SIPPs.