



**Staffordshire**  
**Pension Fund**  
Local Government Pension Scheme

# Pension Tax Training

November 2018

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HYMANS  ROBERTSON



## 1.5 million savers ‘face 55pc pension tax’

More than 1m savers are at risk of paying 55pc pension tax because they will ‘save too much’ in their lifetime, new figures suggest.

*The Daily Telegraph, 20 January 2016*

## Fears of cut to pension tax relief as bill hits 50bn

The government’s bill for pension tax relief has passed £50 billion for the first time, prompting fears that tax relief will be overhauled,

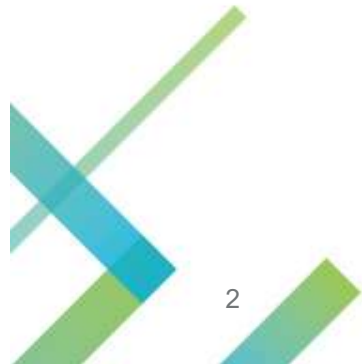
*Charles Walmsley, Citywire, 9 October 2017*

## Hundreds of thousands drift towards costly pensions tax trap

*The Daily Telegraph, 7 March 2017*

## Pensions tax burden shifts back to higher earners

*Willis Towers Watson, 14 October 2017*



# What we will cover



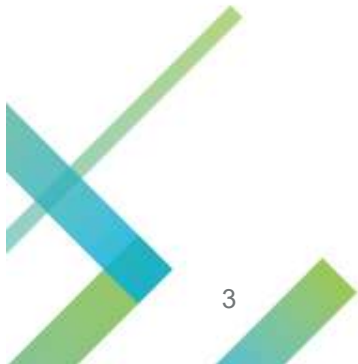
## ✓ Annual Allowance

- ✓ Brief history lesson
- ✓ Standard example + scheme pays
- ✓ Tapered annual allowance + scheme pays
- ✓ Carry-forward
- ✓ Housekeeping

## ✓ Lifetime Allowance

- ✓ Summary
- ✓ Protections
- ✓ Example
- ✓ Tax

**?** Questions **?**



# A brief history lesson

# A look back in time.....



## Pre April 2006

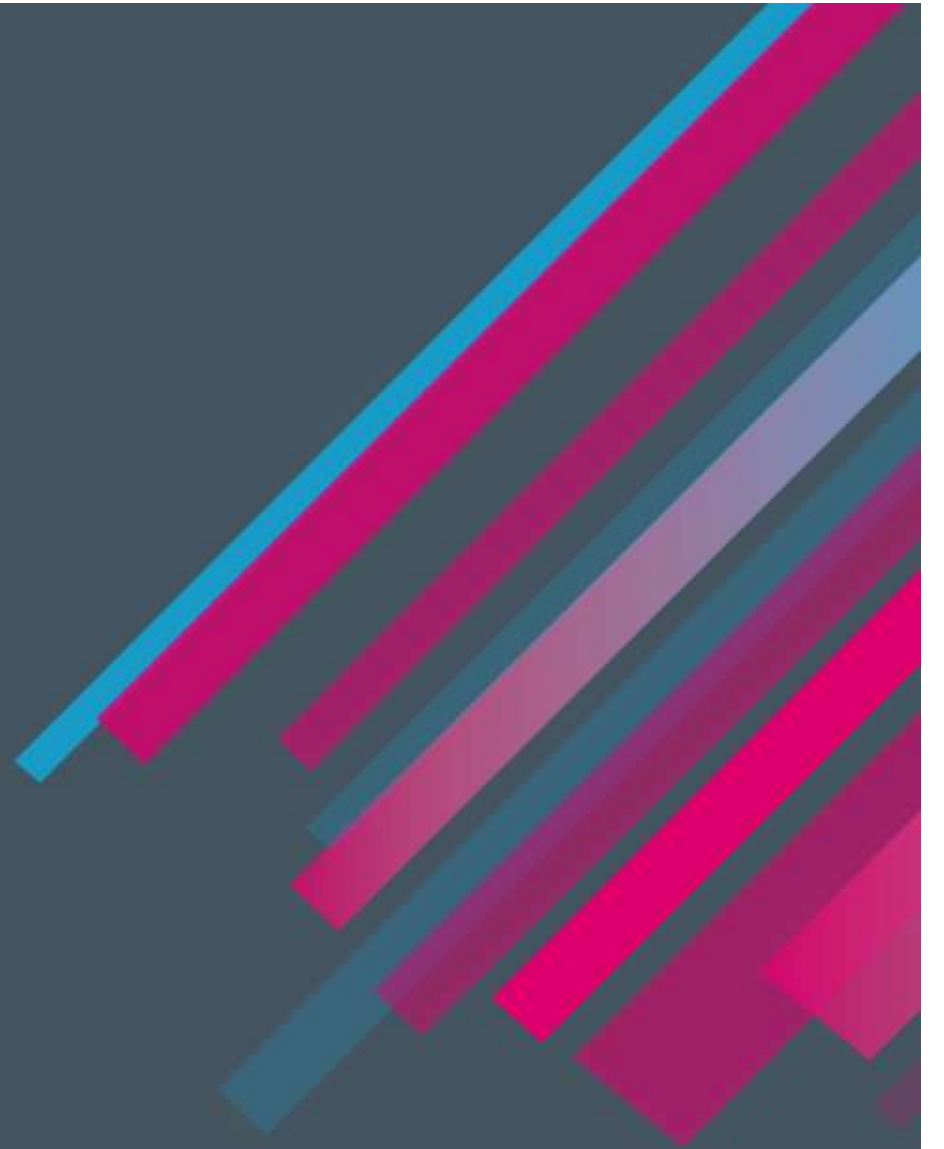
- 8 “regimes”
- Employee contribution restrictions
- Benefits limited on cessation
- Earnings cap in place
- Complex to explain

**A  
Day**

## Post April 2006

- Tax ‘Simplification’
- Removal of previous restrictions
- Introduction of Annual and Lifetime Allowance
- Thresholds – not limits
- Taxed on “excess”
- Increasingly complex ever since

# Annual Allowance Summary



# Annual Allowance



- Value of tax efficient pension saving over the Pension Input Period (currently 6 April – 5 April)
- Allowance for the revaluation of previous years' benefits in line with CPI
- Flat factor of 16 used to value increase in Defined Benefit pension accrual
- Carry forward 3 years of unused allowance
- Full tax-relief up to the Annual Allowance (marginal rate charge above) – I will pick this up later



# Annual Allowance

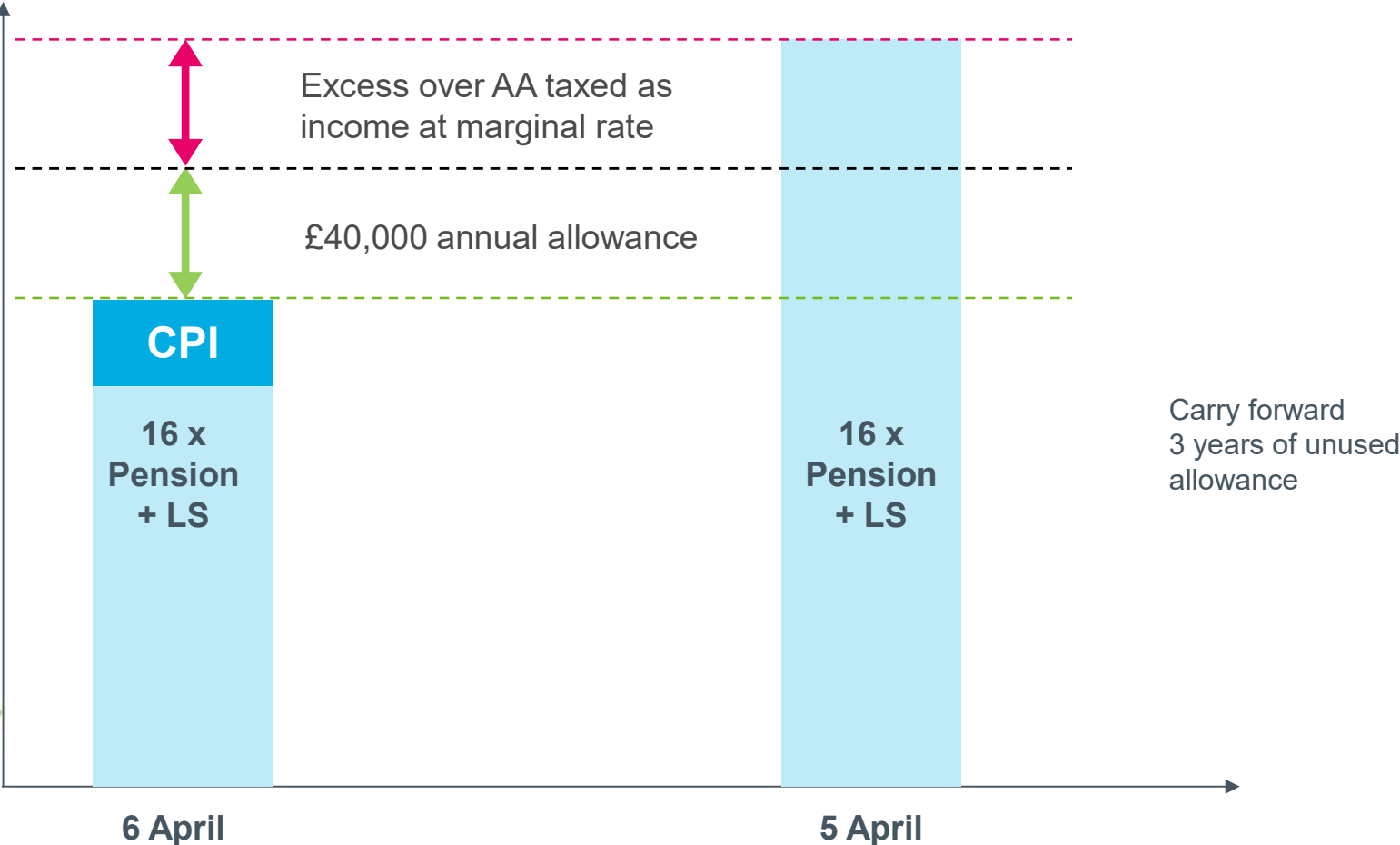


Tax year	Annual allowance
2006/07	£215k*
2007/08	£225k*
2008/09	£235k*
2009/10	£245k*
2010/11	£255k*
2011/12 to 2013/14	£50k
2014/15	£40k
2015/16	£40k (split PIP)
2016/17 – 2018/19	£10k - £40k
2019/20	£10k - £40k





# Standard Annual Allowance



Carry forward  
3 years of unused  
allowance



# Annual Allowance

Example - Standard



# Example – Annual Allowance



## Assumptions:

- 23 years' pensionable service at 5 April 2017
- Final salary at 5 April 2017: £80,000
- Final salary at 5 April 2018: £85,000
- CPI uplift for previous year's benefits: 1%

# Calculation of the value of benefits

## Step 1 – Start of PIP

- 6 April 2017
- Pay = £80,000
- Pension           £26,937
- Lump sum       £42,000
- Value at start of PIP:  
 $16 * £26,937 + £42,000 = £472,992$
- Plus CPI
- $£432,000 * 1.01 = £477,721$

## Step 2 – End of PIP

- 5 April 2018
- Pay £85,000
- Pension           £30,048
- Lump sum       £44,625
- Value at end of PIP:  
 $16 * £30,048 + £44,625 =$   
**£525,393**

## Step 3 – Compare for Growth

PIA:  $£525,393 - £477,721 = £47,672$   
Excess subject to charge:  $£47,672 - £40,000 = £7,672$

# Calculation of tax rate to apply



## Step 4 – Calculate marginal tax rate

• Gross income	£85,000
• Less contributions	<u>£ 8,415</u>
	£76,585
• Plus excess over £40,000	<u>£ 7,672</u>
• Total taxable income	£84,257
• Marginal tax rate is 40%	

# Calculation of tax



## Step 5 – Apply tax rate to excess

• Total growth	£47,672
• Less annual allowance	<u>£40,000</u>
• Excess	£ 7,672
• Apply tax rate @ 40%	£3,069

Assumes no carry forward allowance available

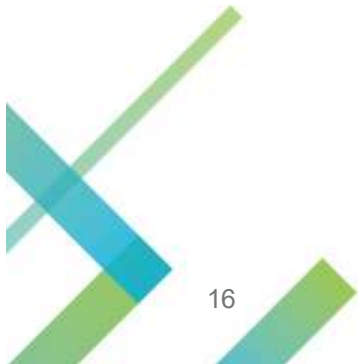
# Annual Allowance

## Scheme Pays Option

# Mandatory Scheme Pays Option



- Pension savings in excess of £40,000
- Charges > £2,000 Member can elect for scheme to pay whole amount.
  - Results in ongoing reduction to annual pension
- Scheme only obliged to pay if whole charge relates to that scheme





# Scheme Pays Option



## Calculate pension deduction

• Gender	Male
• Age	57
• Normal Retirement Age	66
• Scheme pays reduction factor	12.81*
• Tax Charge	£3,069
• $£3,069/12.81 =$	£240
• Revised Pension	£29,808

(\*GAD age related factor adjusted to reflect retirement before NPA of 66 =  $13.63 * 0.94$ )

# Annual Allowance

Tapered Annual Allowance



# Budget(s) 2015 – Tapering Annual Allowance



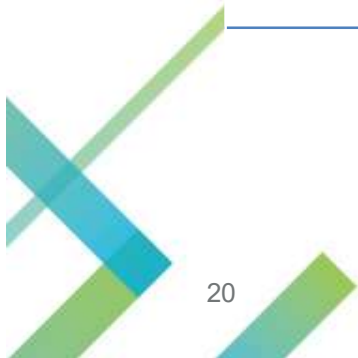
- Tapering of Annual Allowance
  - From 2016/17, Annual Allowance tapers from £40,000 to a minimum of £10,000
- **Threshold Income** is broadly income less gross employee pension contributions
  - Returning Officer, Pay in lieu, Ex Gratia, unpaid leave
  - Other complexities in assessing threshold income (not covered here)
- **Adjusted Income** is Threshold Income; plus the pension input amount
  - Need to work out PIA for the year before being able to determine if tapering applies

# Budget(s) 2015 – Tapering Annual Allowance



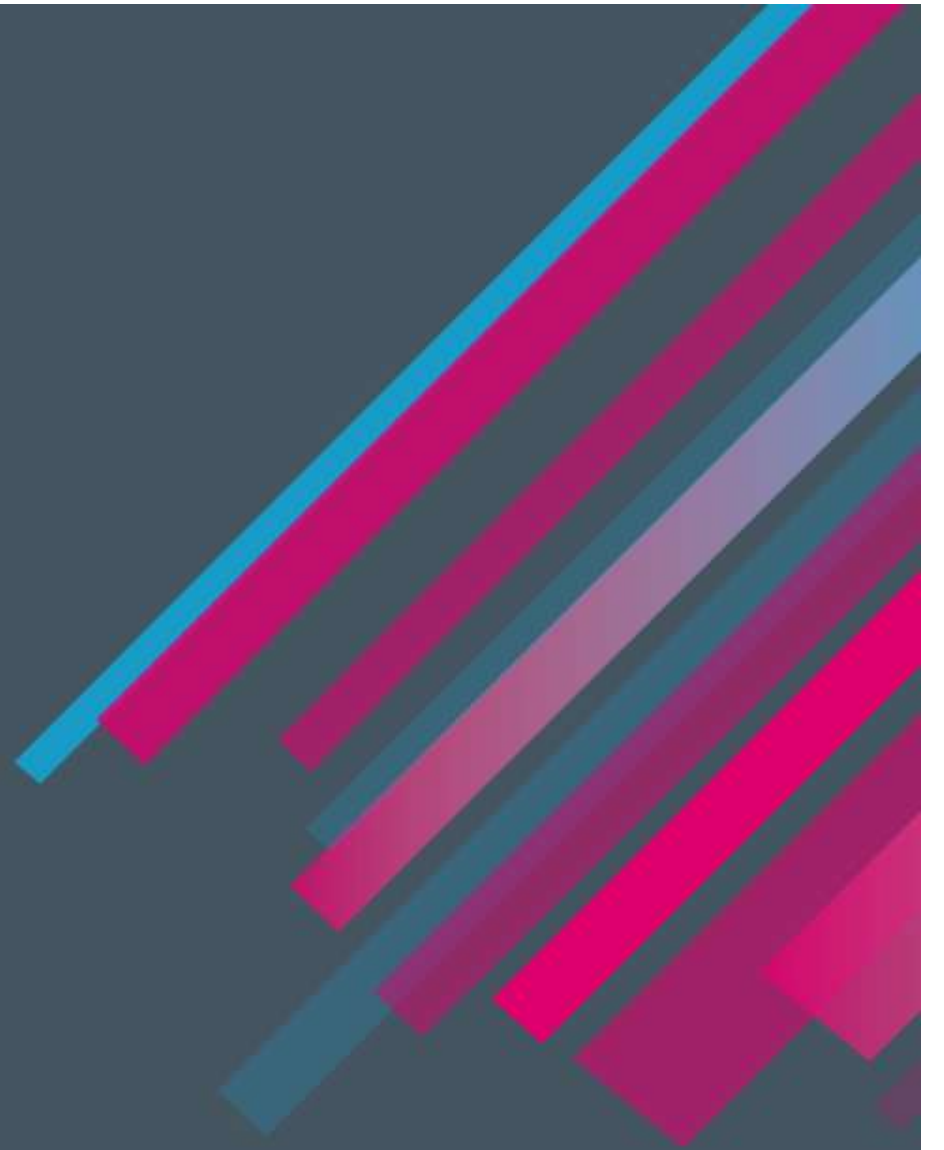
- £1 reduction in AA for every £2 of “**Adjusted Income**” above £150,000 to £210,000
- Only applies if “**Threshold Income**” is above £110,000 (i.e. gross income of around £124,000)

Adjusted Income	AA
< £150k	£40k
£150k	£40k
£180k	£25k
£200k	£15k
£210k	£10K



# Annual Allowance

Example - Tapering



# Member details

## Assumptions:

- 23 years' pensionable service at 5 April 2017
- Final salary at 5 April 2017: £120,000
- Final salary at 5 April 2018: £130,000
- CPI uplift for previous year's benefits: 1%
- Pension Input amount: £87,851

# Does the taper apply?

Is **Threshold Income** above £110,000?

## Step 1 – Threshold Income

- Taxable income = £130,000
- LGPS contribution = £14,820
- **Threshold income** is taxable income less LGPS contributions
- £130,000 - £14,820 = **£115,180**

**Threshold income** is exceeded

# Does the taper apply?

Is **Adjusted Income** above £150,000?

## Step 2 – Adjusted Income

**Adjusted income** is **Threshold income** plus Pension Input Amount

- **Threshold income** = £115,180
- Pension Input amount = £87,851
- **Adjusted Income** is £115,180 + £87,851 = £203,031

**Adjusted income** > £150,000, taper applies



# Apply the taper

## Step 3 – Apply the Taper

- £1 reduction in AA for every £2 of **Adjusted Income** above £150,000
- **Adjusted Income** = £203,031
- Reduction =  $(£203,031 - £150,000) = £53,031 / 2 = £26,515$
- Apply the reduction to the standard AA:  $£40,000 - £26,515 = \mathbf{£13,485}$
- Growth over the tapered AA:  $£87,851 - £13,485 = £74,366$

# Calculate the tax

## Step 4– Calculate Tax

- Taxable income plus pension growth over the tapered AA;
  - $£115,180 + £74,366 = £189,546$
- Member falls into 45% tax bracket;
  - $£39,546 @ 45\% = £17,796$
  - $£34,820 @ 40\% = £13,928$

Total Tax = £31,724

# Annual Allowance

## Scheme Pays Option

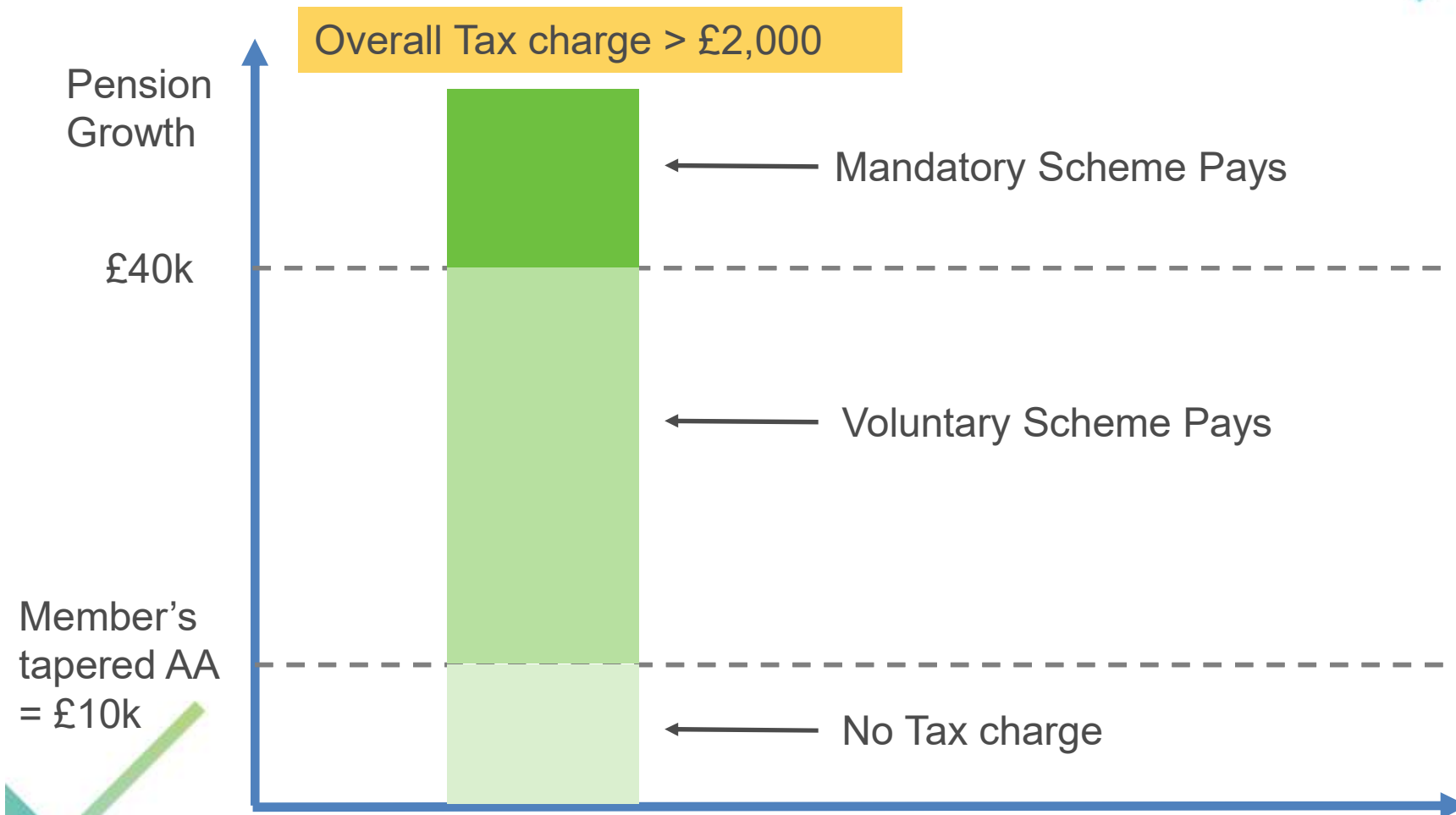
# Voluntary Scheme Pays Option



- Where you are subject to the tapered annual allowance some or all of the tax charge may not be covered by mandatory scheme pays.
- The Fund will have the ability to exercise its discretion.
- Technically no time limit to make voluntary scheme pays election, but the Fund can impose one
  - Also you may be subject to late payment interest if misses self assessment deadline for accounting for and paying tax charge



# Tapered AA and Voluntary Scheme pays



# Annual Allowance

Applying carry forward

# Carry Forward



Year	PIA (£)	AA	Excess in year to c/f (£)
17/18	65,000	40,000	0
16/17	42,000	40,000	0
15/16 pre-alignment tax year	25,000	80,000	55,000 (capped at 40,000). Of the 40,000, 25,000 is needed to c/f to post alignment tax year (e.g. 40,000 – 25,000 = 15,000)
15/16 post-alignment tax year	25,000	0	0
14/15	35,000	40,000	5,000

Excess over AA = £25,000

c/f = £5,000 + £15,000 – 2,000 = £18,000

Total excess over AA = £25,000 - £18,000 = £7,000

# Annual Allowance

## Housekeeping







# Things to consider:

- All pension savings (except State) count towards benefit growth
  - AVCs
  - added years
  - additional contributions
- Impact of “freedom and choice” e.g. money purchase annual allowance (£4,000)
- Declare “scheme pays” on self-assessment tax return
- Salary sacrifice
- Beware “anti-avoidance” for tapered annual allowance

# Mandatory Vs Voluntary Time limits

## Breach in 17/18

Date	Mandatory	Voluntary
6 October 2018	Deadline for administering authority to notify individuals who have exceeded the 17/18 annual allowance in that Fund	
31 January 2019		Tax must be accounted for and paid by this date if there is to be no late payment interest
31 July 2019	The latest date the member may make an irrevocable election to the administering authority	
14 February 2020	The latest date by which the tax relating to the breach may be paid.	

# Late payment penalties & interest



Tax charge amount

Based on number of days late

\* Taken together these penalties can't exceed the tax charge

Missing the filing deadline

3 months late  
6 months late\*  
12 months late\*

£100, plus....  
£10/day – max 90 days  
> £300 or 5% of tax due  
> £300 or 5% of tax due\*\*

\*\* Can increase up to 100% of tax due if deliberately withheld information

Fine for late payment

30 days late  
6 months late  
12 months late

5% of tax due  
5% of tax due  
5% of tax due

Interest

3% p.a. (@ 21 November 2017)

# Lifetime Allowance

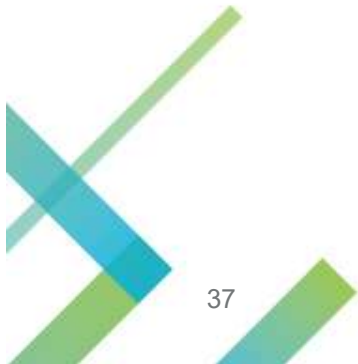
## Summary



# Lifetime Allowance - summary



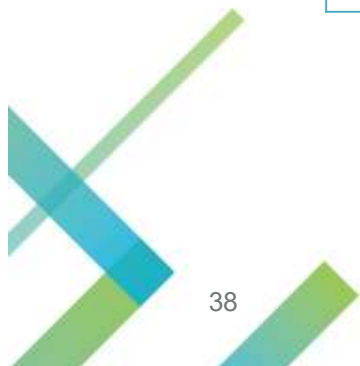
- Value of tax efficient pension saving over a lifetime
- Flat factor of 20 used to value pension accrual
- Then add on lump sum taken
- Includes all pension savings (except state benefit)
- LTA tax-charges – value of excess pension, taxed at 25%



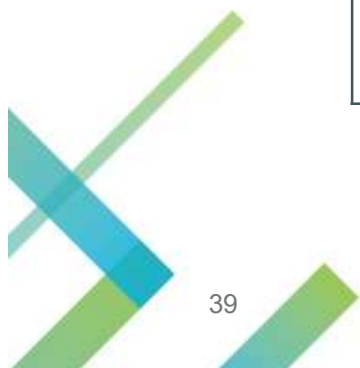
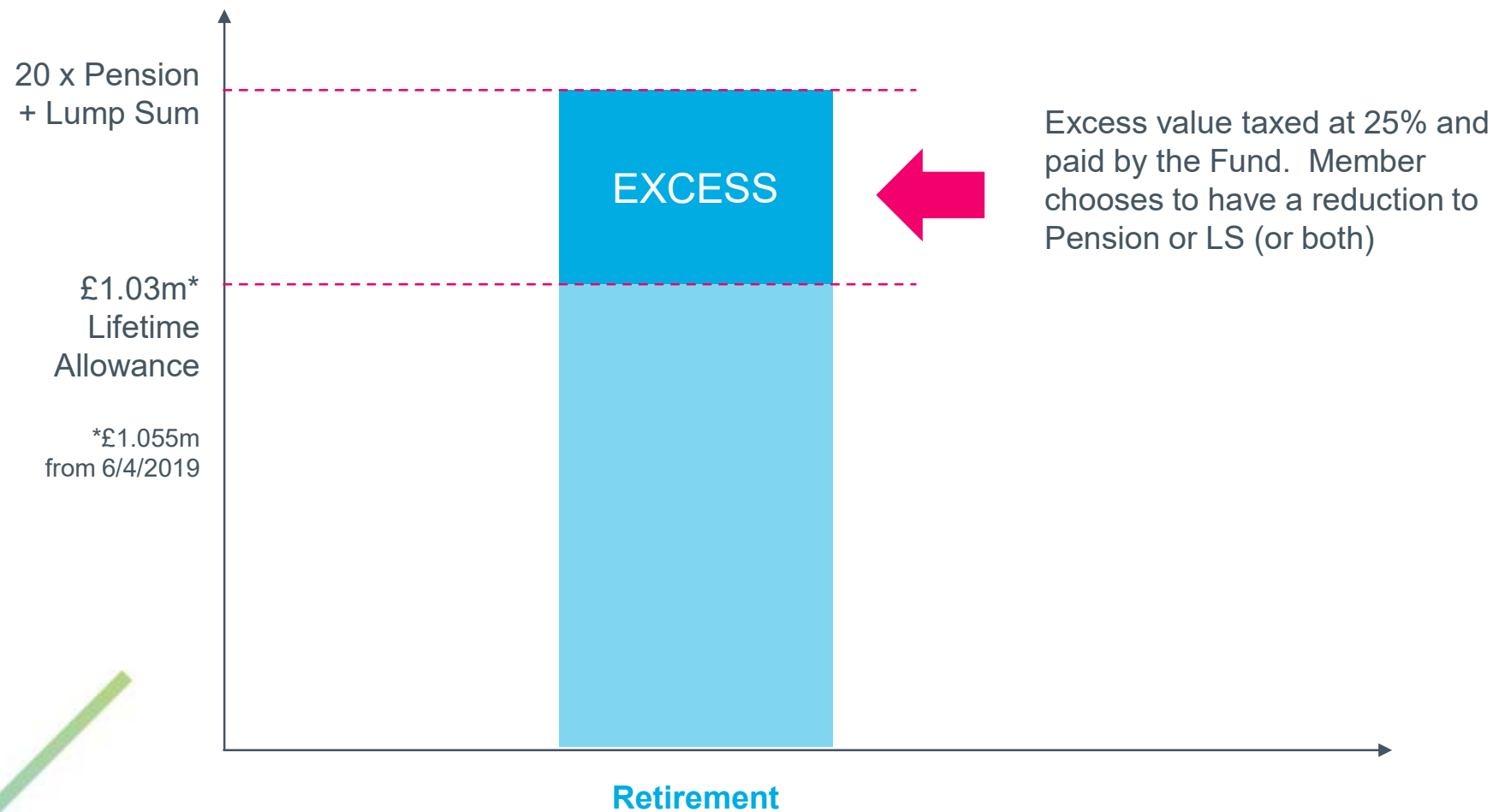
# Lifetime Allowance – from 2006



Tax year	Lifetime Allowance
2006/07	£1.50m
2007/08	£1.60m
2008/09	£1.65m
2009/10	£1.75m
2010/11 to 2011/12	£1.8m
2012/13 to 2013/14	£1.5m
2014/15 to 2015/16	£1.25m
2016/17 to 2017/18	£1m
2018/19	£1.030m
2019/20	£1.055m



# Lifetime Allowance



# Calculation of benefits for Lifetime Allowance

## Lifetime Allowance

**Pay: £150,000**

**Service: 25 years**

Pension = £54,214

Lump Sum = £90,000

value =  $20 * £54,214 + £90,000 = £1,174,280$

Compare to the Lifetime Allowance LTA

$£1,174,280 > £1,030,000$  – tax charge



# Lifetime Allowance Protections

# Historic protections.....if you have them

Type	Protection
Enhanced protection	Value of benefits < or > £1.5m at 5 April 2006, but limits on future benefit accrual
Primary protection	Individual LTA factor applied to current LTA, with no limit on future benefit accrual
Fixed protection 2012 & 2014	£1.8m (2012) or £1.5m (2014), but with very strict limits on future benefit accrual
Individual protection 2014	Value of benefits at 5/4/2014 (max £1.5m), with no limit on future benefit accrual

# The latest protections



Type	Protection
Fixed protection 2016	£1.25m, but with very strict limits on future benefit accrual
Anyone can apply – but you may have already breached	
Individual protection 2016	Value of benefits at 5/4/2016 (max £1.25m), with no limit on future benefit accrual
Must have benefits in excess of £1m at 5 April 2016	

# Applying for new protections



- IP16
  - Pre April 2006 pension in payment £
  - Post April 2006 pensions in payment £
  - Uncrystallised rights £
  - Non UK rights £
  - Declaration does not hold PP or IP14
- FP16
  - Declaration does not hold EP, PP, FP12 or FP14
- HMRC will provide a reference number
  - [www.gov.uk/log-in-register-hmrc-online-services](http://www.gov.uk/log-in-register-hmrc-online-services)
- Lifetime allowance protection history on-line

# Lifetime Allowance

## Example

# Example – Standard lifetime allowance

## Assumptions:

- 28 years' pensionable service at 31 March 2019
- Pensionable salary of £140,000 p.a. @ March 2019
- Lifetime allowance = £1,030,000
- Male aged 57
- LTA debit factor 19.79

# Example – Standard lifetime allowance

## Standard Benefits

### Before Tax

Pension:  
**£58,035**

Lump sum:  
**£89,250**

### After Tax

Pension:  
**£55,256**

Lump sum:  
**£89,250**

Capital value: **£1,249,964**

Tax charge: **£54,991**

## Maximum Lump Sum

### Before Tax

Pension:  
**£44,014**

Lump sum:  
**£257,500**

### After Tax

Pension:  
**£42,653**

Lump sum:  
**£257,500**

Capital value: **£1,137,780**

Tax Charge: **£26,949**

# What about protections?

- ▶ The value of the members benefits @ 6 April 2016 were;
- ▶ Pension: £49,464
- ▶ Lump Sum: £89,250
- ▶ Capital value:  $20 \times £49,464 + £89,250 = £1,078,530$
- ▶ Capital value exceeds £1m, so the member applies for Individual Protection 2016



# Example – IP2016

## Standard Benefits

Before Tax

Pension:  
**£58,035**

Lump sum:  
**£89,250**

After Tax

Pension:  
**£55,870**

Lump sum:  
**£89,250**

Capital value: **£1,249,964**

Tax charge: **£42,898**

**Tax saving: £12,093**

## Maximum Lump Sum

Before Tax

Pension:  
**£43,003**

Lump sum:  
**£269,632**

After Tax

Pension:  
**£42,357**

Lump sum:  
**£269,632**

Capital value: **£1,129,709**

Tax Charge: **£12,794**

**Tax saving: £14,155**

# Lifetime Allowance Tax

# Paying the tax



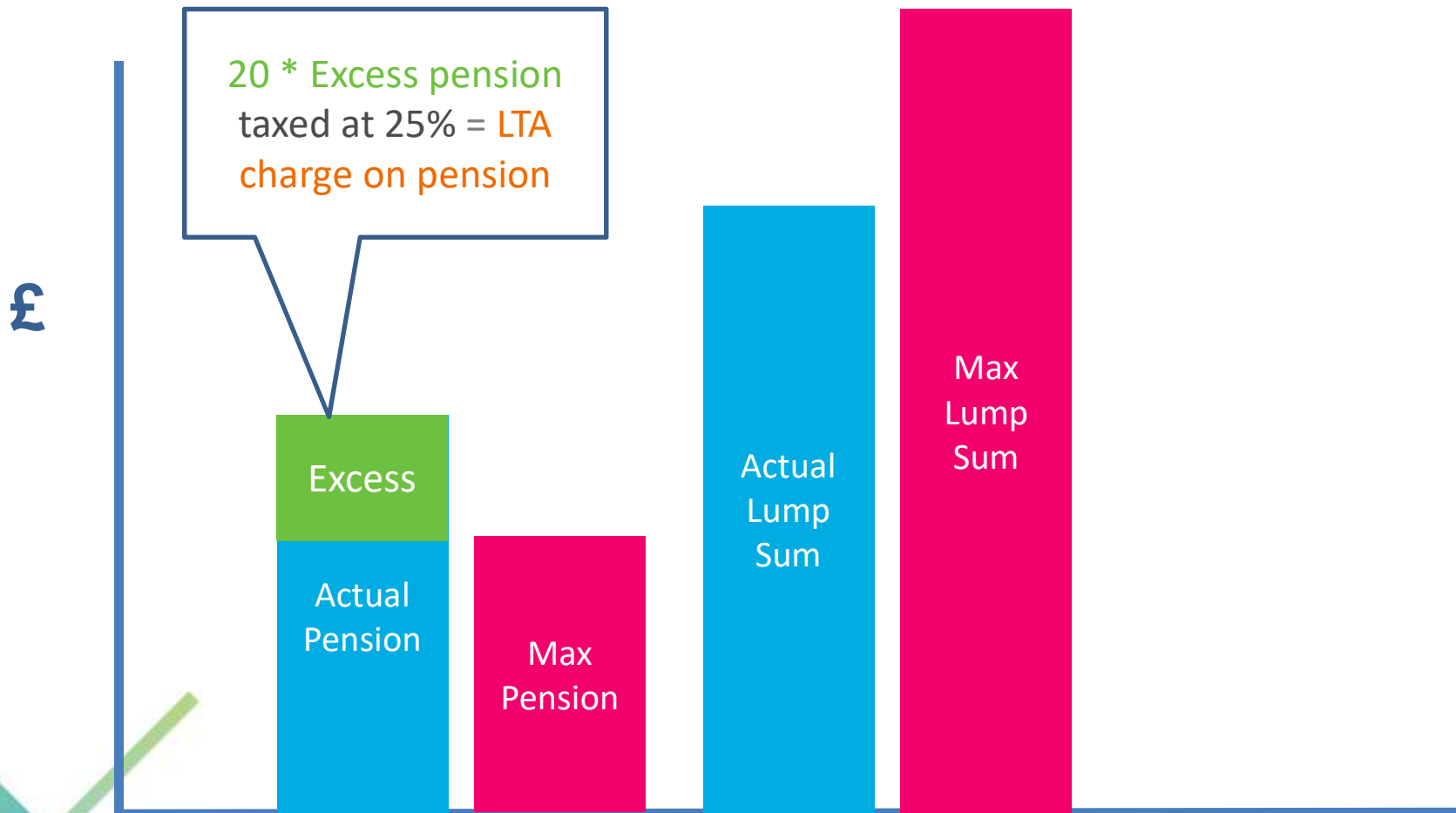
## Option 1

- Excess pension value is calculated, taxed at 25% and paid from Lump Sum

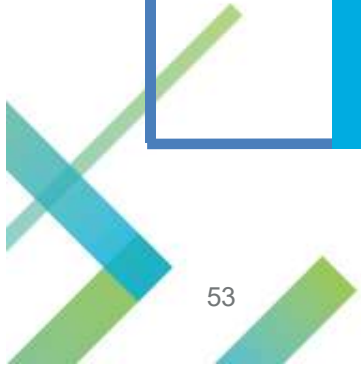
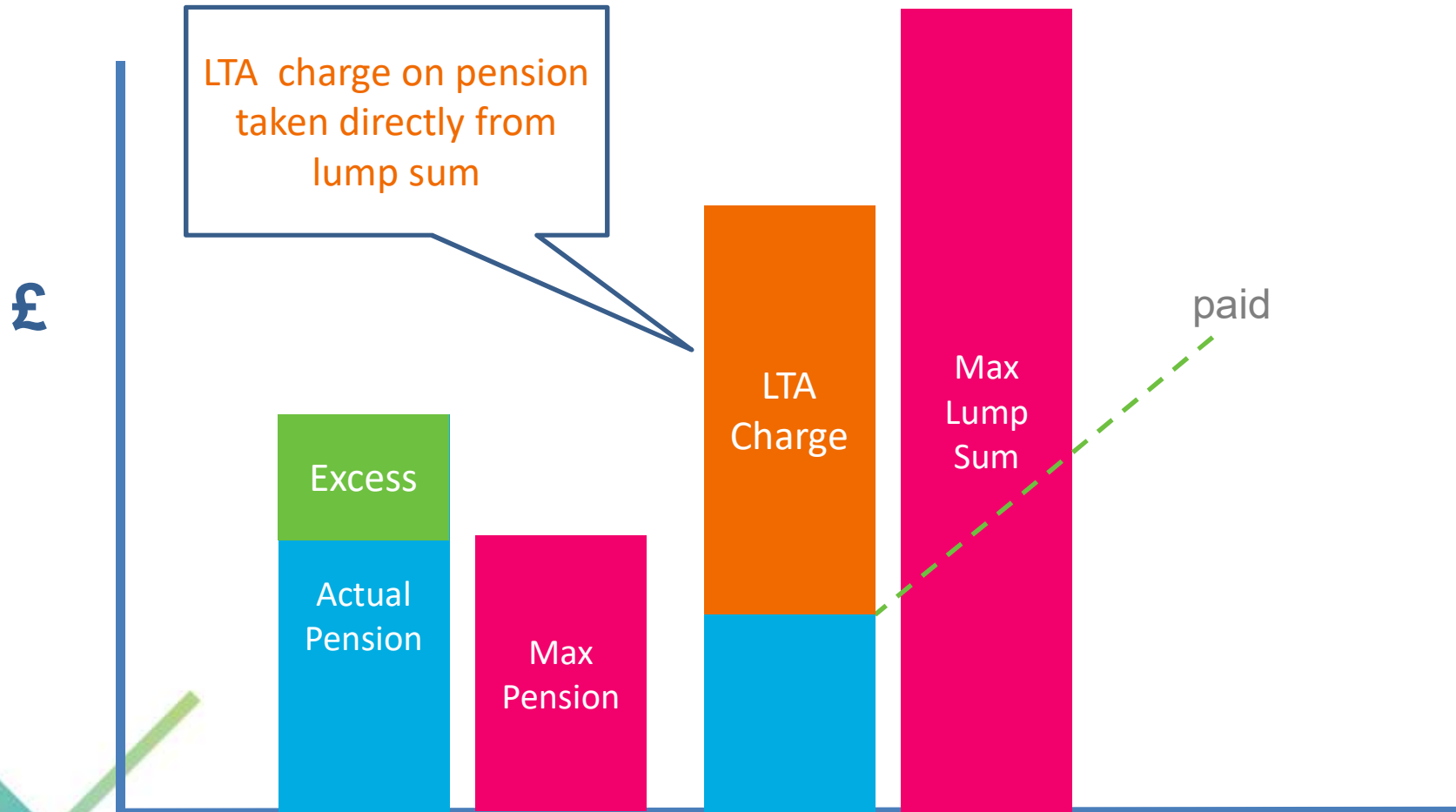
## Option 2

- Excess pension value is calculated, taxed at 25% and paid from pension by means of Scheme Pays option

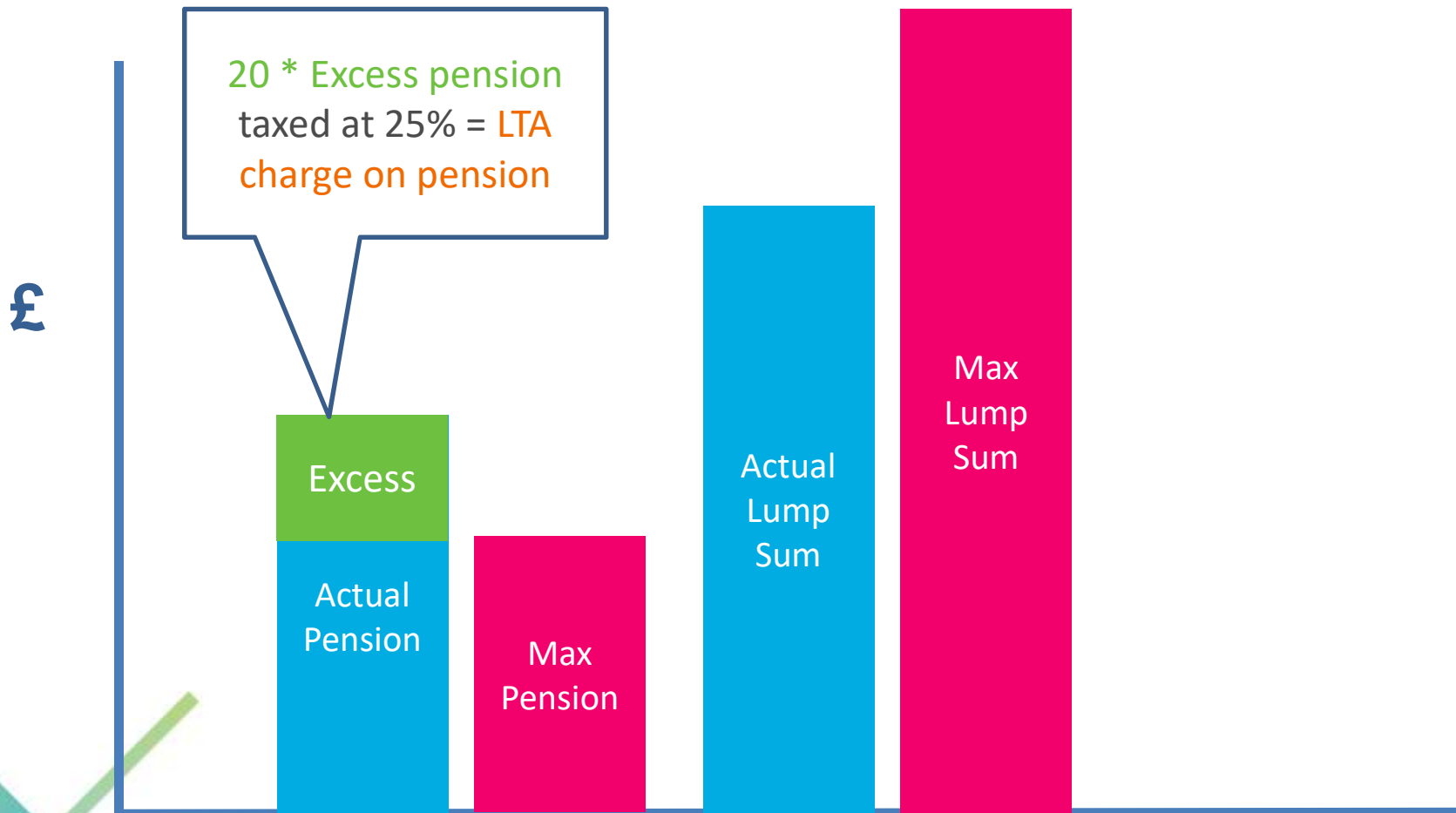
# Option 1



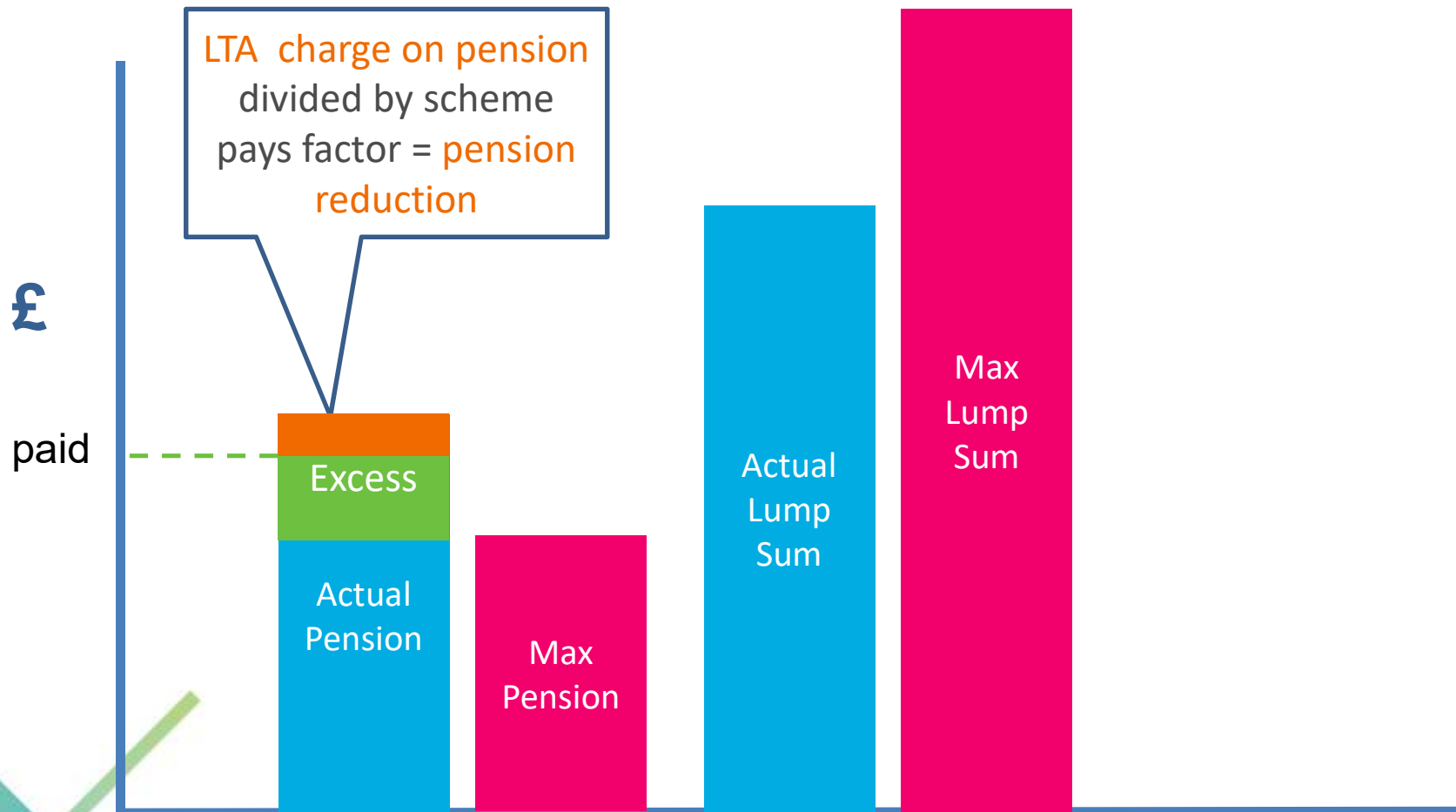
# Option 1



# Option 2



# Option 2



# Lifetime Allowance

## Issues to Consider



# Issues to consider

- Remain in scheme – no change to accrual, but accept tax charge
- Move to 50/50 – half contribution and half future accrual, could reduce or remove tax charge. Annual allowance implications too
- Opt out
  - Save contributions and maybe reduce tax charges on excess
  - Loss of redundancy benefits
  - Loss of ill health/life-cover
  - Impact of CPI v career progression

# General thoughts



- For members with significant past service, estimating future Annual Allowance charges likely to be difficult
  - Depends on relationship between CPI and pay awards
  - Possibility of building up carry forward in years where pay awards frozen or very low
- Due to this uncertainty - opting out on account of paying annual allowance charges alone probably unwise
  - Moving to 50/50 section allows you to benefit from future pay rises/promotion and build up carry forward in meantime
  - If paying both annual and lifetime allowance then opting out may appear more tax efficient



# Better Outcomes



- The Fund will inform you if you breach the *standard* LTA or *standard* AA
- You have responsibility to tell the fund if you are affected by the taper
- Tell the Fund about protections
- Be informed e.g. training events, Fund communications
- Know the timescales
- Appreciate complexity of the calculations
- Undertake modelling and seek Financial advice

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**Early engagement is key**

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Thank you

# Disclaimer



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