Pension Scheme Tax Changes

Changes to the tax regime which applies to occupation and personal pension schemes from April 2014.

There are a number of changes taking place to the tax advantages available to a person from being a member of a pension scheme. These changes are taking place from 6th April 2014.

Such changes are a personal taxation matter and persons affected by some of these changes may need to register themself with HMRC to avail themself of the protections available in relation to the Lifetime Allowance changes.

What changes are being made?

Basically two changes are being made to the tax advantages available from membership of a pension scheme 1) the Lifetime allowance is being reduced and 2) the Annual Allowance is being reduced, both with effect from 6th April 2014. These changes will limit the tax benefits available from pension scheme membership to some individuals. The majority of employees will not be affected by these changes. The changes are aimed at limiting the "tax breaks" high earner can obtain from pension scheme membership. These changes will however impact upon some employees who are at the higher end of the earnings scale or are paying significant amounts of extra contributions or AVC's into their pension plan.

Changes to the Lifetime Allowance

From 6th April 2014 the Lifetime Allowance, the total amount or value which a person can have in all pension schemes before they suffer a tax penalty at retirement, is reducing from £1.5 million to £1.25 million. Clearly these are large sums and this change will only impact upon a limited number of employees. In a defined benefit scheme, such as the LGPS, where we do not hold individual fund values for employees, HMRC determine the overall value of a person's pension by multiplying it by 20 and adding to that the amount of any lump sum payable.

Example - a person who is entitled to an annual pension of £60,000 and a lump sum of £180,000 would have a total fund value of £60,000 x 20 = £1,200,000 + £180,000 = £1,380,000. In this case they would exceed the new reduced Lifetime Allowance limit of £1,250,000 and would be liable for an additional tax change, a "Lifetime Allowance Charge".

Protections Available.

HMRC have announced that there will be 2 protections available to people who may be impacted on by this change to the Lifetime Allowance.

Fixed Protection 2014

To access Fixed Protection an **employee must personally** make an application to HMRC ***before 6th April 2014.*** This is a personal taxation matter and the Pension Section cannot assist with this or advise individuals.

If you apply for Fixed Protection this would mean that you would still be able to have pension rights with an overall value of £1.5 million before you would suffer a Lifetime Allowance charge at retirement.

You cannot have the new “Fixed Protection 2014” if you have obtained from HMRC Primary, Enhanced or Fixed Protections at the time of one of the previous changes to the pension tax regime.

If you apply to HMRC for Fixed Protection 2014 you would lose it if you:-

- Have a contribution paid to any money purchase pension scheme (i.e. a scheme where the pension is ultimately determined by the value of the invested fund rather than by reference to your pay and length of service).
- Build up further benefits in a defined benefit scheme (such as the LGPS or other public sector scheme) above certain limits.
- Join a new pension scheme.
- Start saving in a new pension pot either under your current pension scheme or a new arrangement (e.g. start an AVC arrangement).

Individual Protection 2014.

As well as Fixed Protection 2014 the Government have also announced that Individual Protection 2014 will be available from April 2014 when the Lifetime Allowance reduces to £1.25 million.

- Individual Protection will give you a Lifetime Allowance equal to the value of your pension rights on 5th April 2014 up to a maximum of £1.5 million e.g. if the value of your pension rights on the 5th April 2014 were £1.4 million that would be your individual Lifetime Allowance should you obtain this protection.
- You would **not** lose your Individual Protection by making further savings or contributions to your pension scheme. However, if as in the previous example, the person had pension rights worth £1.4 million on the 5th April 2014 at retirement they would suffer an Annual Allowance Charge in respect of any further pension right they earned in their pension scheme from April 2014.

Any individual who wishes to obtain Individual Protection 2014 can apply to HMRC for it   from 6th April 2014. An application for fixed protection must be made by 5th April 2017.

Individual Protection is not available to persons who obtained Primary Protection 2006 when the Life Time Allowance was first introduced. Individual Protection is however available to persons who obtained Enhanced Protection 2006 from HMRC.

Persons can apply to HMRC for both Fixed Protection 2014 and Individual Protection 2014.

Further information is available on the HMRC web site **http://www.hmrc.gov.uk/pensionschemes/news.htm**

Annual Allowance Tax Charges

The Annual Allowance is the amount by which the value of a person's pension rights can grow **in one year** before they incur an additional tax charge. The Annual Allowance is currently £50,000 but will reduce to £40,000 from 6th April 2014.

This is an example of how the Annual Allowance works for a person in a defined benefit pension scheme such as the LGPS:-

A person has 25 years in the LGPS. At the year ended 31st March 2014 their accrued annual pension was £14,000 and their lump sum £40,000. During the year ended 31st March 2015 the person gets a large pay increase and their accrued annual pension at 31st March 2015 is now £19,000 plus an accrued lump sum of £54,000.

In this case the value of the accrued pension befits for the purposes of the annual allowance limit has increased as follows:-

£19,000 less £14,000 = £5,000 x16	= £80,000
Plus the increase in the lump sum (£54,000 less £40,000)	= £14,000
Increase in the value of the LGPS pension rights	= £94,000

As the increase exceeds the current annual allowance for 2014/15 of £40,000 by £54,000 this employee could possibly be looking at a tax charge on the £54,000 increase in the overall value of their LGPS pension rights.

Please Note - this is a simplified example, in practice inflation is taken into account when comparing the value of accrued pensions in one year with the next and the person would have been able to carry forward any unused annual allowances from the previous 3 years to offset their tax bill.

Important - AVC's.

AVC's also count in the calculation of **all** pension tax limits i.e. in the Annual Allowance example if this person had paid £5,000 in AVC's in that year their pension rights would have grown in value by £99,000 (£94,000 + £5,000 AVC's) and potentially they would have to pay tax on £59,000. In the Lifetime Allowance example if the person had paid overall £60,000 in AVC's the value of £1,380,000 would have increased to £1,440,000 and this would have increased the person's Lifetime Allowance tax charge.

State Pension Rights

The value of your State Pension rights is **not** taken into account for the purposes of assessing any tax liability under either the Lifetime or Annual Allowance.

Important - Please Note

This note has been prepared for general information only and individuals should not rely on the information given. If you have any concerns with regard to your tax position in respect of either the Lifetime or Annual Allowance you should contact HMRC and consider taking independent financial advice. The County Council will not accept any liability for any tax liability incurred by any employee or pension scheme member. It is a person's individual responsibility to apply to HMRC, should they wish to avail themself of either Fixed or Individual Protection 2014 and where appropriate declare any tax payable under the Annual or Lifetime Allowance via the Self-Assessment tax system.

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