

HUBBARD LLOYD PENSIONS TAX NEWSLETTER

6 April 2011 saw the commencement of the new rules on pension tax relief introduced by the coalition government. The new regulations, for some, may result in a tax charge arising on pension contributions. It applies to all pension policies which must be looked at collectively when considering the implications.

Some employees of the NHS will have the benefit of a final salary pension scheme but for GP's who are still technically in a defined benefit scheme the Career Average Revalued Earnings will form the basis of the pension entitlement.

We have therefore compiled this newsletter to inform you of the main changes and who we and the NHS pensions agency feel is most likely to be affected. It does however need to be borne in mind that Royal Assent to the proposals will not be given until July and therefore the following notes relate to the proposed legislation.

Summary of new rules

- Tax relief on pension "contributions" restricted to an "Annual Allowance" of £50,000.
- Any excess above £50,000 will be subject to a tax charge. Whether this is at 40%, or a marginal rate has yet to be finalised. Where the tax charge is over £2,000 and relates to the NHS Pension Scheme members may sign an irrevocable election to ask NHS pension to pay this charge. The members pension and lump sum will be reduced and discussions are currently under way on the method of this calculation.
- For defined contributions schemes i.e. private pensions, it is fairly simple in that if your GROSS contributions exceed £50,000 you will be subject to the tax charge on any excess.
- For defined benefit schemes the £50,000 limit is measured against the yearly growth in your pension accrual benefit and then multiplied by growth factor of 16 plus the growth in the lump sum, and any excess is subject to a tax charge.
- Any unused Annual Allowance can be carried forward for up to 3 years. This also includes the previous 3 years, so any unused allowance from 2008/09 to 2010/11 can be utilised in 2011/12.
- The Lifetime allowance will be reduced from £1.8m to £1.5m with effect from 6 April 2012. The old limit of £1.8m equates to a yearly GP pension of £78,260 where three times pension is taken as a lump sum. The new £1.5m limit equates to a yearly GP pension of £65,217.
- Once the lifetime allowance limit has been breached you will be subject to a 25% tax charge on the excess which will in turn reduce your GP pension.

Who is likely to be affected?

- It is difficult to say this early on but we have been advised that the following categories have a higher risk of being affected:
 - Those in their 50's will be prime candidates
 - Those receiving a very large promotion, especially coupled with long pensionable service
 - Tier 2 ill health retirements
 - Consultants awarded Clinical Excellence Awards, again, especially coupled with long pensionable service

- High earning mental health officers who have service of 20+ years.
- Those paying added years.
- Based on earnings initial estimates for those in the NHS pension scheme who may be effected are:
 - Up to £100,000 – less than 1%
 - £100,000 - £150,000 – about 1/3 of members
 - £150,000 + – 90% plus
- Obviously this is not a comprehensive list and there may well be many others who may be caught.

The table below is taken from the NHS pension agency website and demonstrates who might be affected if pay increases by 5% from the start of the year and inflation is at 3%.

		Pensionable salary at start of tax year								
		100,000	110,000	120,000	130,000	140,000	150,000	160,000	170,000	180,000
Pensionable service at start of tax year	10	Green	Green	Green	Green	Green	Green	Yellow	Red	Red
	15	Green	Green	Green	Green	Green	Yellow	Red	Red	Red
	20	Green	Green	Green	Green	Yellow	Red	Red	Red	Red
	25	Green	Green	Green	Yellow	Red	Red	Red	Red	Red
	30	Green	Green	Yellow	Red	Red	Red	Red	Red	Red
	35	Green	Yellow	Yellow	Red	Red	Red	Red	Red	Red
	40	Green	Yellow	Red	Red	Red	Red	Red	Red	Red

	Pension growth unlikely to be above reduced annual allowance
	Pension growth may be above reduced annual allowance
	Pension growth likely to be above reduced annual allowance

Examples

Below is a simplified example of how it will affect a full time GP partner in a high earning practice who is 54 years old assuming there is no brought forward unused allowance.

	£
Dynamised career earnings to date	3,600,000
Annual pensionable profits	155,000
Annual pension	54,000

Resulting annual increase in pension	2,926
Multiply by growth factor of 16	46,816
Increase in tax free lump sum (3 x pension)	8,778
	55,594

In this instance the GP has exceeded the annual allowance by £5,594, but they may have unused annual allowance brought forward from 2008/09 to offset against this. If not there will be a tax charge on this amount.

We can also show how the self assessment tax payments are likely to be affected by the changes in the tax legislation and these new rules, with the figures below including the pension tax adjustment:

	£
31 July 2011	26,834
31 January 2012	32,896
31 July 2012	28,855
31 January 2013	38,482
31 July 2013	32,064

This GP has gone from paying a relatively constant tax payment of £27,000/£28,000 to a one off sum of nearly £39,000 in January 2013 yet their profits have not increased.

Our second example below is how it can affect an employed individual who receives a pay increase during the year:

Salary 05/04/11	£130,000
Service	30 years
Pension	£65,000
Salary 05/04/12	£160,000
Service	31 years
Pension	£82,666
Pension at start of year (increased in line with inflation)	£67,015
Pension at end of the year	£82,666
Increase in accrued pension benefit	£15,651 x 16 = £250,416

In this example, by getting an increase in salary of £30,000 they have exceeded their annual allowance threshold by £200,416 which would be subject to a tax charge. You can clearly see the tax charge will far outweigh the additional salary.

Practical Implications

The annual allowance calculations can only be finalised when all pay details are available. The filing deadline for superannuation certificates is 28 February following the NHS year but tax returns need to be submitted by 31 January.

The consequences of this, for those who may be affected, will be the need to complete an estimated/provisional tax return, and therefore amongst other things the implication of interest, and possible penalties charged by HMRC, on late paid tax. The tax calculations will then have to be amended when final details are known.

New deadlines have been set by HMRC to try and accommodate the changes and whilst these may be practicable for salaried employees they do not work well for GP's. By the 6 July after the end of the tax year pay details need to be provided to NHS pensions who will then automatically produce statements for those over the annual allowance of £50,000 in the NHS Pension Scheme. The time scale for this will be by 6 October except for 2011/12 the deadline is extended by a year to 6 July 2013. This date is clearly after the filing deadline for the tax return.

Where NHS pension statements are requested there are time limits for the delivery of these but we understand they will contain sufficient information for tax return purposes. A member is however only entitled to one free statement per year. The first year that a request can be made for is 2011/12.

Conclusion

Whilst this newsletter is designed to provide you with a summary of the new rules it will no doubt raise as many questions as it endeavours to answer. What is however clear is that early consideration of the implication of the new rules would be beneficial and with your authority we can obtain information from the Pensions agency to check the calculations of your current pension entitlement and perform the "number crunching" although it will also be necessary to include and take advice on what options are available to you from an FSA regulated firm/individual.

We would be pleased to discuss any of the above further with you either collectively (i.e. as a practice) or individually when you could determine the scope of any assistance you require from us. As we have hopefully set out within this newsletter the proposed legislation is likely to have implications for a considerable number of NHS employees/self employed contractors when completing tax returns.