Housing Bulletin – September 2018

Annual Allowance – A limit on pensions tax relief

In the last few weeks, affected pension scheme members will have received Pension Savings Statements for the 2017/18 tax year. In our experience, these statements are not well understood. This isn't surprising as pensions tax is a very complicated business!

What is a Pension Savings Statement?

Pension scheme members who have breached the £40,000 Annual Allowance in the tax year 2017/18 will receive a statement, which will include a table looking something like this:

Pension input period(s) ending in tax year	Aggregated pension input amount (£)	Standard Annual Allowance (£)
5 April 2018	This column will show an individual's pension savings in each period	£40,000
5 April 2017		£40,000
9 July 2015 to 5 April 2016		£40,000*
31 March 2015 to 8 July 2015		£80,000
5 April 2015		£40,000

* Lower limit applies where pension savings were more than £40,000 in previous pension input period.

But what does this actually mean? Is there a tax charge to pay? Should affected members opt out of workplace pension saving? Is there anything the employer can do?

What is the Tapered Allowance?

Those with a Threshold Income* above £110,000 might have a lower annual allowance. For every £2 of Adjusted Income** above £150,000, the Annual Allowance is reduced by £1 but with a minimum Annual Allowance of £10,000.

* Threshold Income is all taxable income excluding pension savings

** Adjusted Income is all taxable income including pension savings

How do I calculate my pensions savings?

For a Defined Contribution ("DC") scheme, this is pretty straightforward.

DC: Total pension contributions paid over the year by both the employee and employer.

For a Defined Benefit ("DB") scheme, it's a little trickier and you have to use this formula:

DB: Factor of 16 × (Accrued pension at end of year
less accrued pension at start of year, increased by CPI inflation)

Why have some staff breached the Annual Allowance in the first place?

In short, it's because the value of the individual's pension savings over the tax year was greater than £40,000 (or the tapered allowance if lower). This can happen for a number of reasons, for example:

- The pension scheme has generous accrual rates (e.g. LGPS 1/49th or SHPS 1/60th)
- A big increase in pay – perhaps due to a recent promotion
- Long pension scheme membership
- And, perhaps, a combination of all three

It's not just the highest earners who can breach the Annual Allowance

For example, let's take an employee on a salary of £55,000 with 10 years' past service in a 1/60th Final Salary scheme. If they are promoted to a position with a salary of £65,000, then they can breach the Annual Allowance (assuming CPI of 2.5%).

DB:	Factor of 16 × (11 / 60 × £65,000 less 10 / 60 × £55,000 × 1.025) **> £40,000**

How First Actuarial can help

We can help affected staff, most likely members of senior management and the executive team, understand their tax position – for example, whether they are affected by the tapered annual allowance – and how to calculate their tax bill.

On the employer side, a common request is to assess how overall pension strategy fits with the pensions tax system in order to offer a benefit package that works for all.

Need help with your pension strategy?

To discuss your pension strategy, or any other pension matters, please contact your usual First Actuarial consultant, or any one of our nationwide team of housing consultants.

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