

## Abolition of higher rate relief for higher earners

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I have now had the opportunity to study the reams of paperwork which came out from HMRC following the Budget on 22 April and the following guidance should cover most of the situations which will arise for clients. At present legislation is still in draft and could be amended as it goes through parliament. I have commented below on areas where this might happen.

### To whom does the “Special Annual Allowance Charge” apply?

Anyone with **taxable income** (NB not earnings) in the 2007/08 and /or 2008/09 and/or 2009/10 tax years of £150,000 or more.

If they increase their ‘normal regular pensions savings’ after 22 April 2009, and their total ‘annual pensions savings’ exceed £20,000.

### How is the £150,000 ‘relevant income’ calculated?

Earnings from employment  
Earnings from self-employment  
Pensions in payment (including state pension)  
Interest, dividend income, rental income  
Income from a trust

*Plus* pension contributions made under ‘net pay’ arrangements (i.e. member contributions deducted from salary – not employer contributions)

*Less* allowable business losses and gift aid donations

*Less* up to £20,000 relievable pension contributions

*Plus* any salary sacrifice agreed after 22 April 2009

Two examples might help:

Paul’s total earnings in 2008/09 were £140,000. In addition he had £5,000 of bank interest, £10,000 net rental income from the house he inherited from his aunt, and £3,000 of grossed-up dividend income. His total earnings were therefore £158,000. However he paid £800 net per month to a PP, giving £12,000 gross relievable contributions in the tax year. For the purpose of pensions his Relevant Income is therefore £146,000. This means that providing that his Relevant Income in 2007/08 was below £150,000 and that his 2009/10 Relevant Income is also below £150,000, he is not caught by the Special Annual Allowance and can pay a single contribution of more than £100,000 and obtain 40% tax relief.

Lesley earns £80,000 p.a. She has £20,000 p.a. of investment income. She pays £1,500 gross per month AVCs and is a member of her employer's non contributory DB scheme. She has agreed a redundancy package with her employer which will give her £100,000 at the end of March 2010. Her Relevant Income for 2009/10 will be £80,000 + £20,000 - £18,000 + £70,000 = £152,000. She had always intended to sacrifice the taxable element of her redundancy payment (£70,000) and have this paid into the pension scheme, but if she now does so she will be subject to the Special Allowance Charge of 20% on £68,000 as she has used £18,000 of her £20,000 annual pensions savings limit. She will also be subject to a limit of £20,000 on contributions in 2010/11 and 2011/12 if she wants to avoid the Special Allowance Charge.

Note that had she taken redundancy on 31 March 2009 she could have had the full redundancy payment paid to pension and her Relevant Income would never get close to the £150,000 limit.

What are 'normal regular pensions savings'? (Remember that if Relevant Income does not exceed £150,000 then this is irrelevant.)

For personal pensions for a contribution to be a 'protected pension input':  
the individual must be an active member of the scheme before 22 April 2009 – or had made a written application to join before then  
contributions must not increase after 22 April 2009 – except 'in accordance with a rate which was expressly agreed before 22 April 2009'  
payments must have been made 'on a quarterly or more frequent basis'  
payments must not stop – or if they do the number of missed payments must be 'insignificant'

The 'quarterly or more frequent basis' was specifically designed to prevent people paying in substantial single contributions in a last ditch attempt to get higher rate relief, but if it is not changed it will catch out people who regularly wait until towards the year end to consider how much they can afford to pay and then do so in a lump sum. HMRC are aware of industry concerns, but any decision would need to be made by ministers. One possibility is that we might revert to the pre simplification definition of 'ordinary annual contributions' as being the annual average of total contributions in the last three years.

### Comment

The Annual Allowance was only introduced 3 years ago, but already it has effectively been reduced to £150,000 – except for those lucky enough to have been paying £20,000 a month before the budget! There will no doubt be some tweaks before the Bill becomes an Act, but it is difficult not to think that this measure will only hasten the demise of pensions in the UK. In 2012 we can all have personal accounts with 8% contributions including basic rate relief, so what more would anyone want?!

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