

## Finance Bill 2010: What it means for Trustees...

The Finance Bill 2010 confirms that from 6 April 2011 “high income” individuals face a new tax, the “high income excess relief charge” (HIERC), on their savings into UK pensions, making pensions considerably less tax efficient for them.

In the run-up to 2011, trustees can expect employers to ask for help investigating who is affected so they can consider whether alternatives to registered pension scheme membership could be offered to them in future. While predominantly a company issue Trustees need to consider how this could impact their scheme. In the longer term, the HIERC could pose significant communication and administration challenges for trustees.

### Identifying who is affected and how?

Many companies are looking at alternative forms of pension for, and other ways to reward, their key employees and are trying to identify who is affected.

### Who is affected?

Scheme members will fall into the “high income” bracket if they have “relevant income” exceeding £130,000 pa and “gross income” exceeding £150,000 pa.

“Relevant income” is total taxable income from **all** sources (including personal income – from investments, properties etc – as well as employment earnings). Pension contributions under net pay arrangements must be included, as must any salary foregone under “salary sacrifice” arrangements and any redundancy/termination payments to the extent they exceed £30,000.

“Gross income” is relevant income plus the individual’s total “pension savings amount” from all their pension arrangements.

The **pension savings amount** is:

- contributions made by the employer to defined contribution (DC) schemes; and
- an assessment of the value of the pension accruing to the individual each tax year in defined benefit (DB) schemes.

The £130,000 pa and £150,000 pa are not expected to increase (e.g. in line with inflation or earnings) in future.

Trustees are well-placed to assist as a key factor is the “pension savings amount” about which they may have key information such as accruing DB pensions. They are also well placed to estimate how the values of DB pensions will be assessed and to understand who/how may become affected by the HIERC in future. They will need to have regard to data protection rules.

The HIERC will be charged on all an individual’s savings into all registered pension schemes. This could include AVCs and any personal pensions the individual has. Where benefits accrue in a staff scheme, with supplemental benefits provided in an executive top-up scheme, all benefits are subject to the HIERC.



### What effect will the new tax have?

The HIERC will:

- restrict tax relief on an individual’s own pension contributions to the basic rate (20%); and
- tax employer contributions and DB pension accrual similarly to a benefit-in-kind, at 30% (50% marginal less 20% basic rate of tax).

The operation of the charge is complicated for those with gross income between £150,000 pa and £180,000 pa, involving tapering rates of tax.

It is unclear at present how benefits provided through non-registered arrangements such as employer-financed retirement benefit schemes (EFRBS) may be affected.

### Information exchange

Employers will have to provide individuals with the pension information they need for their self-assessment return. They will turn to trustees for information such as benefit statements.

### Self-assessment

Individuals will be responsible for providing to HMRC, through the self-assessment system, the information necessary for HMRC to determine the HIERC.

Trustees will have to respond within a statutory deadline (HMRC suggests 3 months from the date when information for P11Ds is normally available). Items such as up-to-date pensionable salaries will be needed for this, so there will also be an onus on employers to provide these promptly. Trustees will need to collaborate with HR teams and third party administrators to design a practical procedure to ensure this exchange of information works smoothly. The number of members potentially affected will be a key factor to consider.

## Professional advice

Actuarial and legal advice may be needed on a number of matters. The valuation of pension accrual for determining DB pension savings amounts is one area. This will involve applying actuarial factors (dependent on age, retirement age and how pensions-in-payment increase) to different tranches of accrued pensions.

## Who pays?

Any HIERC is the liability of the Individual member.

However, if the charge exceeds £15,000, and the member so requests, the trustees will be required to pay it from the pension scheme and reduce the member's benefits accordingly.

Where trustees reduce benefits, to reflect any HERC they pay on a member's behalf, they will need to make sure the reduction is actuarially fair, to that member and others. This may require careful consideration in some under-funded schemes or schemes that are winding-up.

Trustees will also need to be clear about their role in relation to any alternative arrangements the employer decides to offer high income employees in future. They may wish to keep closely involved with the employer's plans as they develop.

## Dealing with disengagement

Key company decision-makers may be affected by the new tax rules and could become less personally engaged with the pension scheme as a result.

Trustees should be prepared to discuss whether this could adversely affect the company's long-term commitment to the pension scheme and explore any implications for decisions on funding and future benefit design.

## Communication

Trustees and employers will need to agree who should communicate with affected, and potentially affected, employees.

The employer's HR or payroll department should take the lead but trustees may wish to be involved to ensure consistency with other pensions-related material (particularly if changes to the pension scheme are underway or in the pipeline).

The scope of the communication needs to be carefully thought out and will probably need to avoid, directly or indirectly, providing financial advice. It may be useful to direct potentially affected employees towards independent financial advice on retirement and tax planning.

Communication will need to be provided in plenty of time for affected employees to plan their pension contributions from 6 April 2011.

## For further advice and information please contact:

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