

Budget 2011

What does it mean for Pensions?

Trustees and employers will welcome the fact that the Chancellor's Budget 2011 raised no further immediate issues for employer-provided pensions. Both can continue focusing on aligning their pension strategy to the new pension tax regime from 6 April 2011. The most significant change is the reduction of the annual allowance for pension saving to £50,000. The Finance Bill 2011 incorporated draft legislation for the reduced annual and lifetime allowance regime and associated changes.

But the Chancellor has signalled some wider Government plans that could have longer-term implications for employer-provided pensions:

State pension reform and abolition of contracting out

The Government plans to replace the current tiered state pensions with a citizen's pension of £140 a week. In connection with this, the facility for defined benefit (DB) pension schemes to contract-out of the current state second pension would have to be abolished. Employers would face increased costs because they would no longer benefit from National Insurance (NI) rebates which can be up to 3.7% of employees' earnings (figures for 2011/12). A Green Paper on state pension reform and accompanying changes will be published shortly. Possible timescales for change are unclear at present.

Integration of operation of income tax and NI

The Government will consult on how income tax and NI could be integrated. Any integration is likely to be some years away and details are scant so potential implications for employer-provided pensions are uncertain at this point. The Chancellor indicated that pensioners would not have to pay NI but there is no guarantee that the current tax efficiency of pension savings will remain entirely unaffected. Would salary sacrifice (which could become more attractive from 6 April 2011 when all NI rates increased by 1%) continue to be attractive?

Restriction of tax relief on employer asset-backed pension contributions

A number of companies with DB pension liabilities have been using assets instead of cash to fund deficits. This reduced pressure on cash that was already constrained. They also potentially gained corporation tax relief on the assets made available to the Scheme.

The Government will consult this Spring on limiting the corporation tax relief on asset-backed contributions by employers to DB pension schemes from April 2012. The Government's aim is to accurately match tax relief to the value of assets allocated to the pension scheme.

If you are implementing structures over the next twelve months you'll need to ensure they work under current rules. The advantages of these structures, such as providing security to the pension scheme and reducing upfront cash required, could in many cases outweigh any less generous tax treatment.



State pension age to rise with life expectancy and public service pension reform moves closer

Future increases in the state pension age will be directly linked to independent assessments of life expectancy. The Government accepted Lord Hutton's recent proposals as a basis for consulting on public service pension reforms - these include a move towards career average revalued earnings (CARE). The discount rate for calculating public service pensions will move to 3% over the consumer price index (CPI), reinforcing the case for increasing average employee contribution rates by 3%. Trustees and employers may wish to investigate whether scheme members will need greater flexibility as to how/when they can access their pension savings as their working lives are extended.

What you need to consider now

A number of the announcements made in Budget 2011 were long-term reforms. In the meantime, employers and employees are left with a lot of new legislation on pensions effective from 6 April 2011, including:

- the reduced annual allowance of £50,000
- the reduced lifetime allowance of £1.5m from 6 April 2012
- pension schemes being required to pay, at the member's request, any tax bill arising due to the annual allowance charge if more than £2,000
- taxation on contributions to unregistered pension scheme due to the disguised remuneration rules, and
- a relaxation of the rules that require members to buy an annuity by age 75.

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