



**HM Revenue  
& Customs**

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**Pension Schemes: Limiting Tax Relief for High Income  
Individuals**

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Guidance for Pensions Industry  
22 April 2009

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<b>Contents</b>		<b>Page</b>
Foreword		<b>3</b>
Chapter 1	Introduction and Overview	<b>4</b>
Chapter 2	Q&A for scheme administrators and pensions practitioners	<b>11</b>
Chapter 3	Q&A for financial advisors	<b>16</b>
Chapter 4	Q&A for employers	<b>18</b>

**This guidance is based on draft legislation which may be amended as it goes through the Parliamentary process. The guidance therefore is also draft and may need to be amended to reflect any such changes.**

**The tax rates referred to in the guidance are those in place on 22 April 2009.**

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## Foreword

This guidance explains the proposed changes to pension scheme legislation announced in the Chancellor's Budget statement on 22 April 2009.

It includes background details and Questions and Answers for pension scheme administrators, practitioners, financial advisors and employers in relation to the availability of higher rate tax relief on pension contributions, for high income individuals.

If you have further queries not covered in this guide, there is a Technical guidance document on the Budget pages of the HMRC website.

<http://www.hmrc.gov.uk/budget2009/>

## Chapter 1

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### INTRODUCTION

#### Background

In his 2009 Budget, the Chancellor announced two changes to tax relief on pension savings for individuals with income above a certain level:

- the Government intends from 6 April 2011 to restrict tax relief for individuals with an annual income of £150,000 or more. Relief will be tapered away so that for those earning over £180,000 relief will be worth 20 per cent, the same as to a basic rate taxpayer, and
- the Government is introducing new rules to apply from 22 April 2009 to restrict higher rate tax relief on pension contributions for individuals. The restrictions will apply to people
  - whose income is £150,000 or higher
  - who change their normal ongoing regular pension savings, and
  - whose total pension savings exceed £20,000.

This will remove the advantage to those individuals of increasing their pension contributions in excess of their normal pattern.

The vast majority of pension scheme members are unaffected by the proposed changes which only apply to individuals with income of £150,000 or more. Of those people, only those who increase their pension savings may be affected, and even then, only if their overall annual pension savings are £20,000 or more, and if they make changes to their normal pattern of pensions savings or to the way in which pensions benefits accrue.

The special annual allowance, which is set at £20,000, sets an upper limit on the amount of additional pension savings for which full tax relief at the higher rates of tax can be given. Tax relief on additional pension savings above the amount of this allowance will be at the basic rate of tax only. The special annual allowance tax charge which restricts relief on additional contributions to basic rate is a charge on the individual, collected via their Self Assessment tax return. The rate of charge is the difference between the highest rate of income tax and basic rate (20% for 2009-10).

Scheme administrators and employers will not be involved actively in the administration of this.

Certain scheme administrators may be affected by requests to refund pension contributions where scheme members have made non-regular contributions. Where scheme rules allow refunds, scheme administrators will be responsible for making net refunds and accounting for tax on them.

This Guide sets out key points that scheme administrators, practitioners, advisors and employers will need to be aware of to understand whether and how the change coming in from 22 April 2009 affects them. It also provides some Questions and Answers.

**Who do the changes affect?**

The vast majority of people will not be affected by these changes.

**The changes will not apply** to anyone whose total annual income is less than £150,000 and was less than £150,000 in the previous two tax years.

**The changes will not apply** even if their total annual income was £150,000 or more if they continue as normal with their existing regular pension contributions and accrual of pension benefits (including any employer contributions) and do not increase these pension savings on or after 22 April 2009.

**The changes will not apply** if their total annual income was £150,000 or more and they increase their pension savings or accrual of pension benefits, provided their overall annual pension savings or benefit accruals are less than £20,000.

HMRC has published more detailed technical guidance on the Budget Day change on the Budget page of our website. <http://www.hmrc.gov.uk/budget2009/>

There is also a guide for individuals which contains worked examples not included in this guide. <http://www.hmrc.gov.uk/budget2009/>

## **The 2009 Budget changes - Overview**

Legislation will be introduced in the Finance Bill 2009, to apply from Budget Day (22 April 2009), which will affect people with an income of £150,000 or more. Those people will in certain circumstances be subject to a special annual allowance tax charge. The special annual allowance sets an upper limit on the amount of non-regular pensions savings for which full tax relief at rates above basic rate can be given.

- The special annual allowance will be set at £20,000 for the tax years before the main change comes into force.
- The special annual allowance tax charge will restrict the individual's tax relief to basic rate on certain of their pension savings.
- The special annual allowance charge will apply if there are any additional or new pension savings compared to previous years, where the individual's total pension savings in the tax year are over £20,000.
- But any normal, regular ongoing pension savings that an individual already had in place at 22 April 2009 will not be affected by the new rules.

Where the special annual allowance charge applies to an individual, all of their pension savings that receive UK tax relief will count towards the allowance. This includes

- all savings in registered pension schemes, whether made by the individual, on their behalf or by their employer, including
  - benefits accrued in defined benefit schemes (these are often referred to as final salary schemes),
  - contributions made to defined contribution schemes (these are often personal pensions where the individual and/or their employer pay contributions into the scheme), and
- savings in non-UK pension schemes that benefit from UK tax relief.

### **Special annual allowance**

This is set at £20,000 for each tax year for individuals who do not have normal regular ongoing pension savings. For others, the £20,000 allowance is reduced by the amount of their normal regular ongoing pension savings.

### **Special annual allowance charge**

If an individual's pension savings in a tax year exceed their special annual allowance, the individual will be liable to a tax charge to recover tax relief above basic rate given on the additional pension savings. They will pay this charge through their self assessment tax return.

### **Combination with existing annual allowance**

There is already an annual allowance for an individual's pension savings. This limits the total tax relief on the increases to an individual's pension saving in any one year. The special annual allowance will run alongside the existing one.

Where an individual's pension savings exceed both allowances, the new tax charge is adjusted to avoid any double recovery of tax relief that might otherwise arise. When the individual completes their tax return, they should deduct the excess over the annual allowance from the excess over the special annual allowance before applying the special annual allowance tax charge. The tax return documents will include guidance on how to do this.

### **Valuing an individual's income for the special annual allowance**

The special annual allowance charge applies to those individuals who have 'relevant' income of £150,000 or more.

For the purposes of the special annual allowance charge 'relevant income' is

- total income for the tax year before pension contributions, personal allowances or any other reliefs or deductions
- less any normal deductions for reliefs (such as trading losses), including deductions for pension contributions but up to a maximum of £20,000
- less any gift aid deductions as per normal.

But in calculating total 'relevant' income, any amount of employment income foregone by salary sacrifice in return for pension contributions or additional pension benefits if the agreement took place on or after 22 April 2009 must be added back.

In deciding if the special annual allowance charge applies for a tax year, the relevant income for that tax year and for the two previous years is taken into account. For example, if the individual's relevant income was less than £150,000 in 2009-10, they

could still be subject to the special annual allowance charge for that year if their relevant income was £150,000 or more in 2007-08 and/or 2008-09.

In 2010-11 similarly, if the relevant income is less than £150,000, the special annual allowance charge will still apply if the individual's relevant income was £150,000 or more in 2008-09 and/or 2009-10.

### **Valuing an individual's pension savings for the new charge**

The value of an individual's pension savings for the special annual allowance will be calculated in a similar way to that for the existing annual allowance.

- For defined contribution arrangements, this generally means the total contributions in relation to that individual, including any from the employer.
- For defined benefit arrangements this means any increase in the value of accrued rights, which are generally calculated by reference to the salary, years of service and the accrual rate, multiplied by 10.

But for the special annual allowance, the period over which pension savings are calculated is 22 April 2009 to 5 April 2010 for 2009-10, and for following tax years, the tax year, 6 April to 5 April.

Any normal regular ongoing pension savings that were in place before 22 April 2009 will not be affected by the new rules. This type of savings will be classed as 'protected pension input'.

Any pension savings between 6 April 2009 and 21 April 2009 will reduce an individuals' special annual allowance, but will not themselves be subject to the special annual allowance tax charge.

### **Normal regular ongoing pension savings**

The special annual allowance charge will apply only to increases to the individual's normal regular ongoing pension savings from 22 April 2009 where the increase was not agreed before 22 April 2009.

Normal regular ongoing pension savings will be known as 'protected pension inputs'. But if you increase your contributions/accrual above that level on or after 22 April 2009, the increase will not be a protected pension input and will be tested against the special annual allowance.

In money purchase arrangements, the protected pension input is

- the annual amount of the individual's total contributions to the arrangement providing that the contributions were made at least quarterly before 22 April 2009, plus
- any increase in the individual's regular contributions that was agreed before 22 April 2009.

In defined benefits arrangements, all pension savings (which are measured by reference to the change in value of accrued benefits from one year's end to the next) are a protected pension input provided that the way the individual's benefits are calculated under the scheme rules does not change on or after 22 April 2009.

### **Refunds of contributions**

Because the new rules have been brought in with immediate effect, people who are above the income limit for the new charge in the year the contribution was made may find that they have inadvertently exceeded the special annual allowance through making non-regular contributions to personal pension schemes (including retirement annuity contracts) and additional voluntary contributions (AVCs). In such cases, if the scheme rules allow, it may be possible for the pension scheme administrator to refund those contributions to the individual. The legislation refers to a refund of contributions in these circumstances as a 'contributions refund lump sum'.

A lump sum payment can qualify as a 'contributions refund lump sum' only if it is paid after the end of the tax year in which the contributions were made. The first year this applies to is contributions made in 2009-10.

If the scheme does pay a 'contributions refund lump sum'

- the scheme administrator will be liable for a tax charge which is designed to recoup the rate at which tax relief was given on the contributions (40% for refunds made in 2010-11),
- the scheme administrator will pay the tax charge with their Accounting for Tax return for the quarter in which the refund was made,
- if the individual has already reported the excess over the special annual allowance charge on their self assessment tax return and later receives a

refund, they will need to amend their tax return so that the correct amount of tax is collected.

## Chapter 2

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### Q&A

#### Scheme Administrators/Practitioners

##### **How will the Budget 2009 changes affect scheme administrators and practitioners?**

The special annual allowance charge may affect you if you have or anticipate having scheme members who are affected by the changes (see the details in the box on page 5).

You may find that affected individuals ask you for a refund of their contributions.

##### **Do I need to do anything?**

- You may wish to consider whether you want to advise members who may be affected by the new additional annual allowance charge of the consequences of increasing their pension savings.
- You may need to check whether the particular pension scheme's rules already allow you to make refunds of contributions in the circumstances described in the proposed legislation and, if not, whether any changes will be made to allow for them.
- Those involved in day-to-day scheme administration may need to alter their systems to identify 'contributions refund lump sums' made under the new legislation.

##### **Will I need to change my IT systems?**

Those involved in day-to-day scheme administration may need to set their systems up to identify 'contributions refund lump sums' made under the new legislation.

##### **Do I have to report anything to HMRC?**

- You do not have to report to HMRC that you have members who exceed the special annual allowance.
- If your scheme allows refunds of member contributions which qualify as 'contributions refund lump sums', you will need to report these payments to HMRC on the Accounting for Tax return (AFT).

- The scheme administrator is liable to a tax charge on the lump sum amount, and must remit the tax to HMRC along with the AFT by the 45th day after the end of the quarter in which the lump sum was paid.
- The tax charge will be at the individual's marginal rate of income tax for the tax year the contribution was originally paid
- As contributions refund lump sums can be paid only after the end of the tax year in which the contributions were made, the first AFT which could potentially be affected is the 30 June 2010 return, which is due by 14 August 2010.

### **What information do I have to provide?**

The information you will need is the number of members who have received 'contributions refund lump sums' and the amount of tax due. The help text for the AFT will be changed to include guidance in completing the boxes.

### **Do I have to report any details to an affected member?**

There are no additional reporting requirements for scheme administrators to members, although you may find individual members may ask you for details of their total annual contributions or increase in their pension rights between 6 April 2009 and 5 April 2010 for 2009-10 and over the tax year (6 April to 5 April) thereafter if they think they may be affected by the special annual allowance. For 2009-10, they may also ask for the breakdown for the pre-22 April period and from 22 April onwards.

### **How do I adjust my Relief at Source (RAS) claim if the scheme has paid a contributions refund lump sum?**

You should **not** adjust your RAS claim. The tax position in respect of the refunded contribution will be adjusted by the tax charge that the scheme administrator accounts for with the Accounting for Tax return.

### **Do we have to wait until the end of the tax year before making any refund of contributions to a scheme member?**

Yes, otherwise it will be an unauthorised payment.

### **The employer has asked for their contributions to be refunded because some of their staff are receiving refunds under the new legislation.**

If you refund an employer's contribution to them, then unless it qualifies as an 'authorised surplus payment' under the normal rules, it is an unauthorised payment. It is only member contributions that can be refunded to the member as authorised

payments under the new legislation. Unauthorised employer payments entail tax charges on the employer and on the scheme administrator.

### **Can affected members still buy added years?**

For members who are affected by the special annual allowance charge, providing the arrangement to buy the added years was in place before 22 April 2009 (Budget Day) contributions to buy added years will not count towards the special annual allowance. If new added years are bought after this date those contributions will count towards the special annual allowance and could be subject to the new tax charges.

### **Are employer contributions included when working out if the special annual allowance has been exceeded?**

Scheme members with money purchase arrangements must take account of employer contributions as well as their own personal contributions when working out whether or not they have exceeded the special annual allowance.

For defined benefit schemes, the amount that is included in the special allowance calculation is the difference in value of benefits accrued between the beginning and end of the tax year. Employer contributions to fund the scheme are not taken into account, in the same way as they are ignored for the purposes of the existing annual allowance.

### **What happens when a company's pension schemes are re-structured, or an employer sets up a new pension scheme?**

Providing that the scheme is either an occupational pension scheme or a group personal pension scheme and is for the benefit of more than 20 employees, then contributions to it or an increase in value of benefits accrued do not count towards the special annual allowance.

### **Does the special annual allowance charge apply in the year the member dies (the original annual allowance charge does not)?**

- Pension savings in a tax year in which the member later dies do normally count towards the special annual allowance.
- But pension savings in a defined benefits arrangement in a tax year in which the member later dies do not count towards the special annual allowance where at the date of death there are at least 20 members whose benefits are accruing or who are receiving scheme pensions under the pension scheme.

**Does the special annual allowance charge apply in the year the member takes ill-health early retirement (the year in which a member retires is not a pension input period therefore the original annual allowance charge does not)?**

- Pension savings in a tax year in which the member later takes ill-health retirement do normally count towards the special annual allowance.
- But pension savings in an occupational pension scheme, public service scheme, or Group Personal Pension Scheme in a tax year in which the member takes ill-health retirement do not count towards the special annual allowance.

**Income tax rates are going up. Are the rates of the pensions tax charges also changing?**

Not immediately. There are powers in Finance Act 2004 to vary the rate for several of the charges by Treasury Order, and the Finance Bill 2009 will include legislation extending that power to the rates for the other charges, again through secondary legislation.

For example, the special allowance charge for 2009-10 is set at 20% (the difference between higher rate and basic rate). When the 50% additional rate comes in for 2010-11, the Government might decide that the special annual allowance rate should go up 30%.

**High earners will be receiving tax relief at basic rate only as a consequence of the pensions changes. Are the rates of the pensions tax charges changing to reflect this?**

Not immediately. There are powers in Finance Act 2004 to vary the rate for several of the charges by Treasury Order, and the Finance Bill 2009 will include legislation extending that power to the rates for the other charges, again through secondary legislation. Once the Finance Bill has received Royal Assent, and the new powers can be used, the Government will consider which rates need changing, by how much and from what dates.

**When will the legislation for the future changes be ready?**

The legislation introducing the further changes to higher rate tax relief will be included in a future Finance Bill. There will be a consultation on the detail of how to implement the changes for that measure.

**What do I need to do between now and then in respect of the future changes?**

You may wish to follow the progress of the consultation and future Finance Bill draft legislation, when more details will be available as to any changes to schemes' requirements in the future.

## Chapter 3

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### Q&A

#### Financial advisors

##### **How will the Budget 2009 change affect advisors?**

The special annual allowance charge may affect you if you have or anticipate having clients who are affected by the changes (see the details in the box on page 5).

##### **Do I need to do anything?**

If you advise clients with income of £150,000 or more this year or in either of the last two tax years, you may wish to set your systems to identify whether they make any additional pensions savings or their annual pension savings exceed the special annual allowance.

##### **Will I need to change my procedures?**

If you advise scheme members with income of £150,000 or more this year or in either of the last two tax years, you may wish to set your procedures up to identify when their annual pension savings exceed the special annual allowance and they make any additional pensions savings.

##### **What if my client has agreed a salary sacrifice, thus reducing their income below £150,000?**

Providing the agreement was in place before 22 April 2009 (Budget Day), then the amount sacrificed will not be included in their 'relevant income' for the purpose of this measure. However any salary sacrifice arrangements entered into on or after 22 April 2009 in return for pension contributions or additional pension benefits will be included for the purpose of calculating income – the higher figure will be used.

##### **My adviser says he has a clever way to reduce my income below the threshold – what are the consequences if I get involved?**

Depending on how your adviser is suggesting this is achieved, you may end being with tax relief restricted to basic rate on some or all of your normal regular ongoing contributions, which would otherwise have been relieved at higher rates of tax.

HMRC will look very closely at all arrangements designed to avoid the tax. We will pursue any such arrangements vigorously and apply the full breadth of sanctions allowed under the law.

**High earners will be receiving tax relief at basic rate only as a consequence of the pensions changes. Are the rates of the pensions tax charges changing to reflect this?**

Not immediately. There are powers in Finance Act 2004 to vary the rate for several of the charges by Treasury Order, and the Finance Bill 2009 will include legislation extending that power to the rates for the other charges, again through secondary legislation. Once the Finance Bill has received Royal Assent, and the new powers can be used, the Government will consider which rates need changing, by how much and from what dates.

## Chapter 4

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### Q&A

#### Employers

**Some members of staff are receiving refunds under the new legislation. Can I as a sponsoring employer also have a refund of the contributions made in respect of those members of staff?**

If you receive a refund of an employer's contribution, then unless it qualifies as an 'authorised surplus payment' under the normal rules, it is an unauthorised payment. It is only certain member contributions that can be refunded to the high-income individual as authorised payments under the new legislation. Unauthorised employer payments entail tax charges on the employer and on the scheme administrator.

**Can affected members still buy added years?**

For members who are affected by the special annual allowance charge, providing the arrangement to buy the added years was in place before 22 April 2009 (Budget Day) contributions to buy added years will count as normal regular ongoing pensions savings. If new added years are bought on or after this date those contributions will count towards their special annual allowance and could be subject to the new tax charges.

**What happens if the company's pension schemes are re-structured, or we decided to set up a new pension scheme?**

Providing that the scheme is an occupational pension scheme or a Group Personal Pension Scheme and is for the benefit of more than 20 employees then contributions to it do not count towards the special annual allowance.