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**PENSION SCHEMES:    LIMITING TAX RELIEF FOR HIGH  
INCOME INDIVIDUALS  
SPECIAL ANNUAL ALLOWANCE**

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**-            A TECHNICAL GUIDE**

**This guidance explains the proposed changes to pension scheme legislation announced in the Chancellor's Budget statement on 22 April 2009, when the Government announced that it intends to restrict higher rate tax relief for individuals with an annual income of £150,000 or more with effect from 6 April 2011 and that new rules for this group will apply with effect from 22 April 2009. This guidance is based on draft legislation that was published on 22 April 2009. The guidance therefore is also draft and may need to be amended to reflect any future changes.**

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

[22 April 2009]

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

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## INTRODUCTION

The Government has announced its intention to restrict the availability of higher rate tax relief on contributions to Registered Pension Schemes with effect from 6 April 2011 for people with taxable income of £150,000 or more. Relief will be tapered away so that for those earning £180,000 and over, it is worth 20 per cent, the same as to a basic rate taxpayer.

The Government also announced that legislation will be introduced in Finance Bill 2009 to restrict higher rate tax relief on pension contributions for individuals on incomes of £150,000 or higher that are in excess of their normal pattern prior to the new regime coming into effect. It will do so by introducing a special annual allowance of £20,000 that applies from 22 April 2009 and an associated tax charge. Where an individual:

- has taxable income of £150,000 or more, and
- increases their pension savings from 22 April 2009 beyond their normal regular amount,

then any additional pension savings may be subject to a special annual allowance charge.

The special annual allowance charge will, in effect, recover the higher rate tax relief (but not basic rate tax relief) on certain additional pension savings. Any special annual allowance charge due will be paid through Self-Assessment.

## Chapter 1 - OVERVIEW OF SPECIAL ANNUAL ALLOWANCE

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1.1 The Government has announced that, from 6 April 2011 onwards, it intends to restrict higher rate tax relief on pension contributions for individuals with an annual taxable income of £150,000 or more. In anticipation of this change, it proposes to introduce a special annual allowance charge for pension schemes from 2009-2010 to prevent individuals bringing forward their pension contributions to obtain additional higher rate tax relief in those years.

1.2 The special annual allowance applies only in respect of individuals who:

- have an annual taxable income of £150,000 or more in any of the tax years 2007-08 to 2010-11, and
- increase their pension savings from 22 April 2009 beyond their normal regular pensions savings, and
- whose total annual pension savings, including any increases from 22 April 2009 is greater than £20,000.

1.3 The special annual allowance is a maximum of £20,000 and the allowance for an individual is reduced to take account of their normal regular savings.

1.4 The special annual allowance will apply alongside the current annual allowance. In practice this means that all increases in pension savings – ‘pension input amounts’ - will continue to be tested against the current annual allowance in the usual way. However, any pension input amounts that represent new saving that is taken out by, or in respect of, an individual in the period starting with 22 April 2009 and ending on 5 April 2011 will be tested against the special annual allowance as well.

1.5 Pension input amounts that represent normal, regular, ongoing contributions, or benefit accruals, under arrangements that were in place before 22 April 2009 will not be tested against the special annual allowance. Such pension inputs are called ‘protected pension input amounts’. These pension input amounts will continue to be tested against the current annual allowance in the usual way.

1.6 Some forms of pension savings set up during the 2009-2010 or 2010-2011 tax years, despite being new, will still fall into the category of a protected pension input amount, for example where an employer’s pension arrangements are changed as part of corporate restructuring.

1.7 Pension input amounts that are tested against the special annual allowance are called ‘total adjusted pension input amounts’. These will be pension input amounts that were made only in the 2009-2010 or 2010-2011 tax years but they will not include protected pension input amounts.

1.8 Total adjusted pension input amounts that exceed the special annual allowance will be subject to the ‘special annual allowance charge’. This tax charge for 2009-2010 will be at a rate of 20% on the amount by which the total adjusted pension input amounts for the year exceeds the special annual allowance limit for the respective tax year and will be collected from the individual through their Self-Assessment return.

## 1.9 Total pension input amounts, whether consisting

- only of protected pension input amounts,
- only total adjusted pension input amounts, or
- a mixture of both,

that exceed the current annual allowance will continue to be subject to the current annual allowance charge. There will be still be the existing annual allowance tax charge (at 40% for 2009-2010) based on the amount by which the total pension input amount that exceeds the current annual allowance for the tax year concerned.

1.10 The special annual allowance is much lower than the current annual allowance, given that the current annual allowance for 2009-2010 is £245,000 and £255,000 for 2010-2011. Therefore, it is possible that an individual could have adjusted pension input amounts that are liable to the special annual allowance charge but not be liable to the current annual allowance charge. However, if an individual ever became liable to both the special annual allowance charge and the current annual allowance charge there will be a reduction to the special annual allowance charge to prevent double-charging.

1.11 It is possible that individuals might enter into new pension saving on or after 22 April 2009 without realising that the pension saving is an adjusted pension input amount and that the special annual allowance charge applies in respect of some, or all, of that input amount. To allow for this, tax rules for personal pension schemes (including such schemes as retirement annuity contracts) and for additional voluntary contribution arrangements will be extended to enable, if the scheme permits, a member who is potentially liable to the special annual allowance charge to receive a refund of non protected contributions as an authorised member payment. There will be a tax charge in respect of such a refund (40% for contributions made in 2009-2010 and refunded in 2010-2011) and the scheme administrator of the pension scheme paying the refund will be liable for the charge. Whether such refunds are permitted by the scheme will be a matter for those involved with the management of the scheme.

1.12 The following examples illustrate how the special annual allowance will apply:

Andrew has income of £55,000 in 2007/08, £58,000 in 2008/09, £59,000 in 2009/10 and £60,000 in 2010/11. Since his income is less than £150,000 in all years, he is not affected by the new special annual allowance.

Belinda has income of £158,000 in 2009/10 and has total individual and employer pension contributions of £15,000 in the year. Although her income exceeds the £150,000 threshold, her total contributions are less than £20,000 so she is not subject to the special annual allowance charge.

Christine has income of £158,000 in 2010/11 and makes pension contributions of £24,000 during the year of £2,000 per month, something she has done for the previous 2 years. Her income exceeds the £150,000 income threshold. Although her pension contributions are more than £20,000, they will not be subject to the special annual allowance charge because they only reflect her normal regular contributions.

David has income of £170,000 in 2010/11 and makes pension contributions of £50,000. The contributions reflect a regular monthly contribution of £2,000 (as for previous years) and a single payment of £26,000. David's income exceeds the £150,000 income threshold and his pension contributions are more than £20,000. The additional single contribution of £26,000 will be subject to the special annual allowance charge.

## Chapter 2 - SPECIAL ANNUAL ALLOWANCE

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2.1 There will be a special annual allowance for the tax years 2009-2010 and 2010-2011.

### **To what does the special annual allowance apply?**

2.2 The special annual allowance applies in respect of certain new or additional pension saving that is put into registered pension schemes during the 2009-2010 or 2010-2011 tax years. In 2009-2010, it applies for new or additional pension saving that is made in the period beginning on 22 April 2009 and ending on 5 April 2010 only.

2.3 For the purpose of the special annual allowance, the amounts of such new or additional pension saving are called 'total adjusted pension input amounts'.

### **Does the special annual allowance apply to everyone?**

2.4 The special annual allowance does not apply to everyone.

2.5 The special annual allowance applies only to individuals whose taxable income is £150,000 or more in the current tax year or in either of the previous two tax years.

2.6 For the 2009-2010 tax year the special annual allowance will apply to individuals

- whose income is £150,000 or more in any of the 2007-2008, 2008-2009 or 2009-2010 tax years, and
- who have adjusted pension input amounts in 2009-2010.

2.7 For the 2010-2011 tax year the special annual allowance will apply to individuals

- whose income is £150,000 or more in any of the 2008-2009, 2009-2010 or 2010-2011 tax years, and
- who have adjusted pension input amounts in 2010-2011.

### **What about the current annual allowance introduced in 2006?**

2.8 The special annual allowance runs alongside the annual allowance that was introduced from the tax year 2006-2007 onwards for registered pension schemes – the 'current annual allowance'.

### **What about existing pension saving arrangements?**

2.9 The special annual allowance does not apply to normal ongoing pension saving under arrangements that were in place immediately before 22 April 2009. Such amounts of pension saving are called protected pension input amounts and, though

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not tested against the special annual allowance, they will continue to be tested against the current annual allowance.

### **What happens if the special annual allowance is exceeded?**

2.10 If the amount of new or additional pension saving, which is an adjusted pension input amount, exceeds the special annual allowance there will be a special annual allowance charge in respect of the excess amount. The individual scheme member who made the new pension saving is liable to the charge. This includes new or additional pension saving made by the individual, on behalf of the individual (such as by a relative of the member) or in respect of the individual (by the individual's employer).

### **What is the amount of the special annual allowance?**

2.11 The amount of the special annual allowance is £20,000 for both 2009-2010 and 2010-2011. In 2009-2010, it, in effect, applies for the period beginning on 22 April 2009 and ending on 5 April 2010.

2.12 However, the amount of the special annual allowance is reduced by

- pension input amounts called protected pension input amounts, and
- pension input amounts called 'pre-22 April 2009 pension input amounts'.

Protected pension input amounts are the individual's normal regular ongoing pension savings and pre-22 April 2009 pension input amounts are an individual's pension input amounts that relate to the period starting on 6 April 2009 and ending on 21 April 2009.

#### Example

On 6 April 2009 Mark has completed 10 years pensionable service in a scheme where pension benefit accrues on a 1/60th accrual rate. His pensionable salary for that year is £145,000. Accordingly his pensionable entitlement on that date is £24,166 ( $10 \times 1/60\text{th} \times £145,000$ ). A lump sum is available only by commutation of pension.

By 5 April 2010 Mark's pensionable salary had risen to £150,000. Accordingly his pensionable entitlement on that date is £27,500 ( $11 \times 1/60\text{th} \times £150,000$ ).

A capital value is given to Mark's pension rights at 6 April 2009 and 5 April 2010 to determine the amount of increase to those rights. This is done by multiplying the amount of those respective pension rights by a factor of 10.

Mark's pension rights under this arrangement have increased by a value of £33,340 ( $(£27,500 \times 10) - (£24,166 \times 10)$ ). The pension input amount for this arrangement is, therefore, £33,340.

Mark has no other rights accruing under this or any other registered pension scheme, so his total pension input amount is also £33,340.

Part of the pension input amount for 2009-2010 of £33,340 is a protected pension input amount and so that input amount is not subject to the special annual allowance for that year. It is the apportioned part of the input amount that relates to the period beginning with 22 April 2009 and ending on 5 April 2010, the amount being £31,879 ( $349/365 \times £33,340$ ).

Also, the apportioned part of the pension input amount of £33,340 that relates to the period from 6 April 2009 to 21 April 2009, £1,461 ( $16/365 \times £33,340$ ), is not tested against the special annual allowance for that tax year.

However, Mark's special annual allowance for 2009-2010 is reduced by both the amount representing his protected pension input amount for that year and the amount representing the pension input for the period 6 April 2009 to 21 April 2009. His special annual allowance for that year is reduced to nil (as £33,340 exceeds £20,000).

Therefore, if Mark did have any other pension input amounts for 2009-2010 that were not protected pension input amounts or pre-22 April 2009 amounts all of those other input amounts would exceed Mark's special annual allowance limit of nil rather than £20,000. (Any such 'total adjusted pension input amount' would also be tested against the current annual allowance because it would also be part of Mark's total pension input amount under existing tax rules.)

### **What is the tax charge for exceeding the special annual allowance?**

2.13 When an individual has adjusted pension input amounts that exceed the special annual allowance the special annual allowance charge will apply in respect of the excess.

2.14 The special annual allowance charge will be at a rate of 20% in 2009/10 to equal tax relief on pension contributions in excess of the special annual allowance over the basic rate.

2.15 The special annual allowance charge is on the amount of the excess over the special annual allowance.

### **Who is liable for the special annual allowance charge?**

2.16 The special annual allowance charge is an income tax charge on the individual scheme member who has exceeded the special annual allowance.

#### **Example**

For 2009-2010 Mark has income of £150,000 and a protected pension input amount of £33,340 in respect of an existing pension saving arrangement with his employer that was in place before 22 April 2009. That input amount is not subject to the special annual allowance for 2009-2010.

However, Mark's special annual allowance for 2009-2010 is reduced by the amount representing his protected pension input amount for that year. His special annual allowance for that year is reduced to nil (£33,340 exceeds £20,000).

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In 2009-2010 Mark starts a new pension saving arrangement under a personal pension scheme and pays in contributions of £4,000 in that year. This is the only other pension savings that Mark has made for 2009-2010. These contributions mean that Mark has a total adjusted pension input amount of £4,000 for 2009-2010.

Those adjusted pension input amounts have exceeded Mark's special annual allowance limit of nil for 2009-2010. Mark is liable to the special annual allowance charge in respect of the total adjusted pension input amount of £4,000. The amount of the tax charge is £800 (£4,000 x 20%).

### **What happens to the current annual allowance introduced on 6 April 2006?**

2.17 The tax rules for pension schemes changed in 2006 when a new set of rules was introduced for pension schemes that qualify for tax reliefs and exemptions. One of the features of these rules is the annual allowance – the current annual allowance.

2.18 For 2006-2007, the current annual allowance was set at £215,000. Since then it has increased each tax year. For 2009-2010 it is £245,000 and for 2010-2011 it will be £255,000.

2.19 The current annual allowance remains in place.

2.20 Details about the current annual allowance are in the Registered Pension Schemes Manual, RPSM06100000 onwards. The Registered Pension Schemes Manual is available on the HMRC internet site at [www.hmrc.gov.uk](http://www.hmrc.gov.uk).

### **How does the current annual allowance interact with the special annual allowance?**

2.21 The current annual allowance will continue to apply as before in respect of all pension input amounts in respect of an individual. For the 2009-2010 and 2010-2011 tax years in particular the current annual allowance will apply in respect of all pension input amounts whether those input amounts are:

- only protected pension input amounts
- only adjusted pension input amounts, or
- a mixture of both.

2.22 However, the special annual allowance, and the possibility of a special annual allowance charge, will apply only in respect of individuals

- with income of £150,000 or more in the current tax year or in the two previous tax years, and
- who have adjusted pension input amounts in 2009-2010 or in 2010-2011 tax years.

## Enhanced Protection

2.23 The special annual allowance will apply to an individual who has registered to have enhanced protection of pension rights.

2.24 So if an adjusted pension input amount arises, there is a risk that enhanced protection status may be lost.

### Example

In 2006 Paula gave notice to HMRC about her intention to rely on enhanced protection. While she retains enhanced protection, she would not be subject to the lifetime allowance charge. She has a money purchase arrangement (which is not a cash balance arrangement) to which she has not contributed since 2005. Paula's income was more than £150,000 in 2009-2010.

But on 1 May 2009 she paid a contribution of £30,000 to her personal pension scheme. She appreciates that the payment of the contribution has triggered a relevant benefit accrual (see RPSM03104510) leading to loss on enhanced protection. This means that when she comes to take benefits from the money purchase arrangement, she will be subject to a lifetime allowance test in the normal way.

But she asks her scheme if she may be permitted to have a refund of the contribution. The scheme administrator agrees to pay Paula a contributions refund lump sum and does so on 1 May 2010 as the payment cannot be made in the tax year of the original contribution. The scheme administrator deducts tax on the payment.

So the payment of the contributions refund lump sum does not alter the fact that the payment of the contribution led to the loss of enhanced protection. But in arriving at the amount of the total adjusted pension input amount, the payment of the refund contributions lump sum will reduce the amount for the tax year when the original contribution of £30,000 was paid – ie in 2009-2010.

## Chapter 3 - PROTECTED PENSION INPUT AMOUNTS PENSION ARRANGEMENTS IN EXISTENCE IMMEDIATELY BEFORE 22/04/09

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3.1 The special annual allowance applies in respect of new or additional pension savings that are put into registered pension schemes during the 2009-2010 or 2010-2011 tax years; where that new pension saving is made by, on behalf or in respect of an individual with income of £150,000 or more.

3.2 To determine what amount of new or additional pension saving i.e. the total adjusted pension input amount that is made during the 2009-2010 or 2010-2011 tax years the individual's total pension input amounts must be determined for the respective tax year.

3.3 An amount representing 'protected pension input amounts' can then be deducted from that total pension input amount figure.

3.4 One form of protected pension input amount is an amount that represents an individual's 'normal ongoing pension saving' during 2009-2010 or 2010-2011 that relates to pension arrangements that an individual had in place immediately before 22 April 2009.

3.5 The other form of protected pension input amount is that which is still possible despite relating to certain new pension arrangements that were set up on or after 22 April 2009. Such as arrangements commencing as a result of a new employment.

3.6 For 'normal ongoing pension saving' that was in place immediately before 22 April 2009 to be a protected pension input amount it must meet certain conditions. How normal ongoing pension saving qualifies as a protected pension input amount will depend on the type of arrangement and the type of pension scheme under which that arrangement is held. See paragraphs 3.11 onwards

3.7 Normal ongoing pension saving that qualifies as a protected pension input amount will not be tested against the special annual allowance. However, such protected pension input amounts will continue to be tested in the usual way as a pension input against the current annual allowance.

3.8 However, though the input amount is not tested against the special annual allowance, the total amount of protected pension inputs that an individual has in the 2009-2010 or 2010-2011 tax years reduces the available special annual allowance for that individual for the respective tax year.

### Example

Mark's total protected pension input amount in 2009-2010 is £16,000. For the same tax year, Mark's special annual allowance limit is £4,000 (£20,000 - £16,000).

3.9 If a pension input amount made during 2009-2010 or 2010-2011 meets any of the relevant conditions set out in paragraphs 3.11 onwards, as they relate to the particular type of pension scheme and types of arrangements under the scheme, that input amount will be a protected pension input amount.

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## **Anti-avoidance rule for Protected Input Amounts**

### **General**

3.10 All arrangement will cease to be arrangements which create protected pension input amounts if the individual participates in a scheme or arrangement (or schemes or arrangements) which have as their main purpose or one of their main purposes to avoid liability to the special annual allowance charge, the current annual allowance charge or the lifetime allowance charge.

Note - the terms 'scheme' or 'arrangements' are used here in the sense of avoidance devices rather than pension schemes or pension arrangements. Such a 'scheme' or 'arrangement' includes any agreement, understanding, transaction or series of transactions (whether or not legally enforceable).

### **Defined Benefits Arrangements**

#### **Occupational and public service pension schemes**

3.11 A pension input to a defined benefits arrangement is a protected pension input amount where the following conditions are met:

- the arrangement is under a pension scheme that is
  - an occupational pension scheme, or
  - a public service pension scheme
- the individual was accruing benefits under the arrangement during the period that
  - for the purpose of the 2009-2010 tax year, begins before 22 April 2009 and ends on 5 April 2010, and
  - for the purpose of the 2010-2011 tax year begins before 22 April 2009 and ends on 5 April 2011,
  - or ends on such earlier date within the above period that the individual ceased to accrue rights under the arrangement, and
- either on or since 22 April 2009, there has been no material change to the way that benefits are calculated under the arrangement.

3.12 If, on or after 22 April 2009, there is a material change to the way benefits are calculated under a defined benefits arrangement an input to that arrangement following the material change either

- where there is a protected pension input amount to the extent that the amount is not as a result of that material change, or
- where the following conditions are met:
  - the arrangement is under a pension scheme that is

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- an occupational pension scheme, or
- a public service pension scheme
- the individual was accruing benefits under the arrangement on 22 April 2009, and
- there are at least 50 active members of the same pension scheme whose rights are calculated on the same basis as that applying to the individual's arrangement.

Then the pension inputs under that arrangement continue to be protected

### **What are material changes?**

3.13 Material changes are likely to include

- a change in the method of calculating pensionable salary from final salary to yearly salary
- an increase in the accrual rate – for example eightieths to sixtieths, other than as already built-in under the scheme rules
- inclusion of bonuses to pensionable salary where such amounts are capable of being significant amounts, and
- inclusion of total actual service within the calculation of pensionable service, where the scheme previously had a qualifying period for membership of more than 1 year.

### **Which changes are unlikely to be material changes?**

3.14 Changes which are unlikely to be material changes include

- an increase to scheme pensions in payment which brings the level of total increases on the pension in payment to an amount of up to 5% per year or the increase in the Retail Prices Index, and
- changes to the accrual of benefits that do not have a significant effect on the value of the final pension.

#### **Example**

Brenda is an employee of a sponsoring employer of an occupational pension scheme. The employer arranges for the scheme rules to be amended. Previously, the maximum benefits under the scheme have been limited by reference to a cap on the calculation of earnings. But from 6 April 2010 the cap is removed, and consequently Brenda is accruing prospective rights which have been significantly increased. The pension input amount is increased as a direct result. This would be regarded as a material change for those affected.

Under the rules on the special annual allowance, the tests to be applied to see whether the increase in rights may be regarded as a protected pension input amount in the case of Brenda's defined benefits arrangement are:

- is the increase in rights attributable to the change?

It is in this instance, so we need to consider further.

- does the change affect at least 50 active members of the scheme on the same basis?

In this instance the scheme is a fairly large one, and there are 150 scheme members whose rights are increased on the same basis as they are all holding prospective rights with an accrual rate of one-sixtieth using both pensionable service and pensionable salary in the same basis as Brenda's. So the removal of the cap in this scheme, despite being a material change, will not lead to an adjusted pension input amount to be tested against the special annual allowance for Brenda's arrangement. Instead, the increase in rights will give rise to a protected pension input amount which will be tested against the current annual allowance.

### **Contributions to purchase 'added years'**

3.15 Contributions that an individual is paying toward a defined benefits arrangement for the purpose of purchasing 'added years' of defined benefit under that arrangement are protected pension input amounts where:

- the arrangement under which the added years are being purchased was in place immediately before noon on 22 April 2009, or
- the arrangement was not in place immediately before noon on 22 April 2009 but the arrangement is in accordance with a written application made by the individual and that application was received by, or on behalf of, the scheme administrator of the pension scheme before noon on 22 April 2009, and
- on or after 22 April 2009 (or when contributions were first paid), the rate at which contributions are being paid under the arrangement does not increase otherwise in accordance with an increased rate which was expressly agreed before 22 April 2009 (or when contributions were first paid),
- the payment of contributions under the arrangement have been made on a quarterly or more frequent basis, in accordance with terms that were in place before 22 April 2009 (or in accordance with the written application), and
- on or after 22 April 2009 there has been no failure to pay the contributions on a quarterly or more frequent basis, or
- where there has been any failure to pay the contributions on a quarterly or more regular basis, the number of such failures is insignificant. In practice, this can be taken to mean that a small number of occasions of inadvertently missed contributions that do not signify the end of accruing benefits will be accepted as not being a failure for this purpose.

## Money purchase arrangements

### 'Other' money purchase arrangements

#### Occupational and public service pension schemes and group personal pension arrangements

3.16 A pension input to an 'other' money purchase arrangement (a money purchase arrangement that is not a cash balance arrangement) is a protected pension input amount where the following conditions are met:

- the pension scheme under which the arrangement is held is
  - an occupational pension scheme, or
  - a public service pension scheme, or
  - part of a group personal pension scheme;
- the individual was an active member of the pension scheme in relation to the arrangement throughout the period that
  - for the purpose of the 2009-2010 tax year, begins before 22 April 2009 and ends on 5 April 2010, and
  - for the purpose of the 2010-2011 tax year begins before 22 April 2009 and ends on 5 April 2011,
  - or ends on such earlier date within the above period that the individual ceased to accrue rights under the arrangement;
- on or after 22 April 2009, the rate at which contributions are being paid under the arrangement does not increase otherwise than in accordance with an increased rate which was expressly agreed before 22 April 2009;
- the payment of contributions under the arrangement have been made on a quarterly or more regular basis, in accordance with terms that were in place before 22 April 2009;
- on or after 22 April 2009 there has been no failure to pay the contributions on a quarterly or more regular basis, or
- where there has been any failure to pay the contributions on a quarterly or more regular basis, the number of such failures is insignificant. In practice, this can be taken to mean that a small number of occasions of inadvertently missed contributions that do not signify the end of accruing benefits will be accepted as not being a failure for this purpose.

3.17 For this purpose, contributions being paid under the arrangement means contributions paid

- by the individual,

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- on behalf of the individual, and
- in respect of the individual by the individual's employer, or
- by any combination of the above.

#### Example

Immediately before 22 April 2009 Mark had an arrangement in place that meant contributions of £10,000 would be paid every 31 March, 30 June, 30 September and 31 December.

After paying the 31 March contribution Mark was unable to make arrangements for the payment of the 30 June and 30 September contributions. The next contribution that Mark was able to make was the 31 December contribution which was then followed by the next contribution on 31 March 2010.

Although Mark missed two of the four instalments of contributions that would have been paid for the purposes of the 2009-2010 tax year the number of occasions on which the contributions were not paid is insignificant and did not spell the end of accruing benefits. The contributions made on 31 December 2009 and 31 March 2010 are, therefore, protected pension input amounts.

Mark then pays contributions of £10,000 on all of the following due dates of 30 June 2010, 30 September, 31 December and 31 March 2011. All of these contributions are protected pension input amounts for the purpose of the 2010-2011 tax year.

### Cash balance arrangements

#### Occupational and public service pension schemes

3.18 A pension input to a cash balance arrangement (a money purchase arrangement that is not an 'other' money purchase arrangement) is a protected pension input amount where the following conditions are met:

- the pension scheme under which the arrangement is held is
  - an occupational pension scheme, or
  - a public service pension scheme
- the individual has been accruing benefits under the arrangement throughout the period that
  - for the purpose of the 2009-2010 tax year, begins before 22 April 2009 and ends on 5 April 2010,
  - for the purpose of the 2010-2011 tax year begins before 22 April 2009 and ends on 5 April 2011

- or such earlier date within the above period that the individual ceased to accrue rights under the arrangement, and
- there has been no material change to the way that benefits are calculated under the arrangement either on or since 22 April 2009.

3.19 If, on or after 22 April 2009, there is a material change to the way benefits are calculated under a cash balance arrangement an input to that arrangement following that change is a protected pension input amount where the following conditions are met:

- the pension scheme under which the arrangement is held is
  - an occupational pension scheme, or
  - a public service pension scheme;
- the individual was accruing benefits under the arrangement on 22 April 2009, and

either

- the material change applies to at least 50 active members of the same pension scheme under which the arrangement is held and who are affected in the same way as the individual's arrangement, or
- despite there being a material change the amount is not attributable to the material change.

### **Additional voluntary contributions to money purchase arrangements including cash balance arrangements**

#### **Occupational and public service pension schemes**

3.20 Additional voluntary contributions that are being paid to a money purchase arrangement ('other' money purchase or cash balance) are protected pension input amounts where:

- the additional voluntary contributions are being paid in respect of an arrangement under a pension scheme that is
  - an occupational pension scheme, or
  - a public service pension scheme;
- the arrangement under which the additional voluntary contributions are paid was in place immediately before 22 April 2009 or;
- the arrangement was not in place immediately before noon on 22 April 2009 but the arrangement is in accordance with a written application made by the individual and that application was received by, or on behalf of, the scheme administrator of the pension scheme before noon on 22 April 2009, and

- on or after 22 April 2009 (or when contributions were first paid), the rate at which contributions are being paid under the arrangement does not increase otherwise in accordance with an increased rate which was expressly agreed before 22 April 2009 (or when contributions were first paid);;
- the payment of contributions under the arrangement have been made on a quarterly or more frequent basis, in accordance with terms that were in place before 22 April 2009 (or in accordance with the written application), and
- on or after 22 April 2009 there has been no failure to pay the contributions on a quarterly or more frequent basis, or
- where there has been any failure to pay the contributions on a quarterly or more regular basis, the number of such failures is insignificant. In practice, this can be taken to mean that a small number of occasions of inadvertently missed contributions that do not signify the end of accruing benefits will be accepted as not being a failure for this purpose.

### **‘Other’ money purchase arrangements**

#### **Pension schemes other than occupational, public service or group personal pension schemes**

3.21 A pension input to an ‘other’ money purchase arrangement (not a cash balance arrangement) under a pension scheme that is not

- an occupational pension scheme,
- a public service pension scheme, or
- part of a group personal pension scheme,

is a protected pension input amount where the following conditions are met:

- the individual was an active member of the pension scheme in relation to the arrangement throughout the period that
  - for the purpose of the 2009-2010 tax year, begins before 22 April 2009 and ends on 5 April 2010, and
  - for the purpose of the 2010-2011 tax year begins before 22 April 2009 and ends on 5 April 2011,
  - or ends on such earlier date that the individual ceased to accrue rights under the arrangement;
- on or after 22 April 2009, the rate at which contributions are being paid under the arrangement does not increase otherwise in accordance with an increased rate which was expressly agreed before 22 April 2009;
- the payment of contributions under the arrangement have been made on a quarterly or more frequent basis, in accordance with scheme provisions that were in place before 22 April 2009, and

- on or after 22 April 2009 there has been no failure to pay the contributions on a quarterly or more frequent basis, or
- where there has been any failure to pay the contributions on a quarterly or more regular basis, the number of such failures is insignificant. In practice, this can be taken to mean that a small number of occasions of inadvertently missed contributions that do not signify the end of accruing benefits will be accepted as not being a failure for this purpose.

3.22 For this purpose, contributions being paid under the arrangement means contributions paid

- by the individual
- on behalf of the individual, and
- in respect of the individual by the individual's employer, or
- by any combination of the above.

#### **'Other' money purchase arrangements**

##### **Membership applications made to join a pension scheme other than an occupational, public service or group personal pension scheme**

3.23 If an individual is an active member by reference to an 'other' money purchase arrangement that is under a pension scheme that is not

- an occupational pension scheme,
- a public service pension scheme, or
- part of a group personal pension scheme,

but

- the individual was not such an active member immediately before 22 April 2009,

but

- that individual made a written application to become such as active member in relation the arrangement before 22 April 2009,

and

- that written application was received by, or behalf of the scheme administrator of the pension scheme under which the application is held before 12 noon on 22 April 2009,

a pension input into that arrangement will be a protected pension input if the following conditions are met:

- the individual was an active member of the pension scheme in relation to the arrangement throughout the period that begins on the date on which the individual became an active member of the arrangement, and
  - for the purpose of the 2009-2010 tax year, ends on 5 April 2010,
  - for the purpose of the 2010-2011 tax year, ends on 5 April 2011,
  - or ends on such earlier date that the individual ceased to accrue rights under the arrangement,
- on or after the date on which the individual became an active member of the arrangement, the rate at which contributions are being paid under the arrangement does not increase otherwise in accordance with the terms of the arrangement and those terms were in place as part of the written application made before 22 April 2009 and received no later than 12 noon on 22 April 2009;
- the payment of contributions under the arrangement have been made on a quarterly or more frequent basis, in accordance with scheme provisions that were in place as part of the written application made before 22 April 2009 and received no later than 12 noon on 22 April 2009, and
- there has been no failure to pay the contributions on a quarterly or more frequent basis, or
- where there has been any failure to pay the contributions on a quarterly or more frequent basis, the number of such failures is insignificant. In practice, this can be taken to mean that a small number of occasions of inadvertently missed contributions that do not signify the end of accruing benefits will be accepted as not being a failure for this purpose.

3.24 For this purpose, contributions being paid under the arrangement means contributions paid

- by the individual
- on behalf of the individual, and
- in respect of the individual by the individual's employer, or
- by any combination of the above.

## Chapter 4 - PROTECTED PENSION INPUT AMOUNTS

### NEW PENSION ARRANGEMENTS SET UP ON OR AFTER 22 APRIL 2009 AND ARRANGEMENTS RE-ACTIVATED ON OR AFTER 22 APRIL 2009

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4.1 The special annual allowance applies in respect of new pension savings that are put into registered pension schemes during the 2009-2010 or 2010-2011 tax years; where that new pension saving is made by, on behalf or in respect of an individual with income of £150,000 or more.

4.2 To determine what amount of new pension saving is made during the 2009-2010 or 2010-2011 tax years the individual's total pension input amounts must be determined for the respective tax year.

4.3 An amount representing 'protected pension input amounts' can be deducted from that total pension input amount figure to arrive at the total adjusted pension input amount to test against the available special annual allowance.

4.4 One form of protected pension input amount is an amount that represents an individual's 'normal ongoing pension saving' during 2009-2010 or 2010-2011 that relates to pension arrangements that an individual had in place immediately before 22 April 2009. So this will apply to existing arrangements of the individual.

4.5 The other form of protected pension input amount is that which relates to new pension saving arrangements that were set up on or after 22 April 2009 or where arrangements are re-activated on or after 22 April 2009. It is possible for such arrangements to produce protected pension input amounts provided certain conditions are met.

4.6 The conditions that must be met for input amounts are as follows.

4.7 Pension inputs made under an arrangement newly set up on or after 22 April 2009 will be protected pension input amounts where the following conditions are met:

- the new arrangement is under a pension scheme that is
  - an occupational pension scheme,
  - a public service pension scheme, or
  - forms part of a group personal pension scheme;
- the arrangement, except in relation to membership of a public service pension scheme, relates to an employment of the individual;
- the contributions under the arrangement are not additional voluntary contributions or contributions for the purpose of purchasing added years;
- there are 20 or more other arrangements for other members under the same scheme under which benefit accrue on the same basis as that for the arrangement of the individual ;

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. 22

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

- where the arrangement is under an occupational pension scheme or forms part of a group personal pension scheme, those 20 or more other members are employees of the employer who is the employer in relation to the arrangement of the individual;
- there is no material change to the way benefits are calculated under the arrangement in the period beginning with the date on which the arrangement is made and
  - for the purpose of the 2009-2010 tax year, ends on 5 April 2010, or
  - for the purpose of the 2010-2011 tax year, ends on 5 April 2011,
  - or ends on such earlier date that the individual ceased to accrue rights under the arrangement;

4.8 For this purpose an arrangement relates to an employment where

- the earnings by reference to which benefits under the arrangement are calculated are earnings from the employment, or
- the employer in relation to the arrangement pays contributions under the arrangement in respect of the individual.

4.9 It will also be acceptable for the individual to have an arrangement which otherwise meets these conditions where the individual was an employee of the employer, left the pensionable employment but later re-joins the registered pension scheme of the employer and re-activates the existing arrangement. Although the member's arrangement may not be one set up on or after 22 April 2009, it may still qualify.

4.10 Amounts of pension saving under

- new arrangements set up on or after 22 April 2009, or
- arrangements that are re-activated on or after 22 April 2009, and
- that qualify as a protected pension input amounts

will not be tested against the special annual allowance.

4.11 However, such protected pension input amounts will continue to be tested in the usual way as a pension input against the current annual allowance.

4.12 However, though the input amount is not tested against the special annual allowance, the total amount of protected pension inputs that an individual has in the 2009-2010 or 2010-2011 tax years reduces special annual allowance limit for that individual for the respective tax year.

#### Example

Mark's total protected pension input amount in 2009-2010 is £16,000. For the same tax year, Mark's special annual allowance limit is £4,000 (£20,000 - £16,000).

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

4.13 See also Chapter 5 which sets out circumstances in which contributions to new and re-activated arrangements do not count as protected pension input amounts.

#### **Anti-avoidance rules for pension input amounts**

4.14 The legislation includes a number of anti-avoidance rules relating to pension input amounts. One applies where arrangements are in place that result in the measurement of the pension input amount being for a higher amount than would otherwise apply. Another more general rule removes protection from pension input amounts if the individual is party to a scheme or arrangement designed to reduce liability to the new special annual allowance charge, or to the existing annual and lifetime allowance charges.

Note - the terms 'scheme' or 'arrangements' are used here in the sense of avoidance devices rather than pension schemes or pension arrangements. Such a 'scheme' or 'arrangement' includes any agreement, understanding, transaction or series of transactions (whether or not legally enforceable).

## Chapter 5 - ANTI-AVOIDANCE RULES

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5.1 The legislation includes a number of anti-avoidance rules relating to pension input amounts. One applies where arrangements are in place that result in the measurement of the pension input amount being for a lower amount than might otherwise apply. Another more general rule removes protection from pension input amounts if the individual is party to a scheme or arrangement designed to reduce liability to the new special annual allowance charge, or to the existing annual and lifetime allowance charges.

### **Manipulating the value of the pension input amount**

5.2 The legislation includes an anti-avoidance rule whereby the measurement of the 'total pension input amount' for the purpose of establishing a 'total adjusted pension input amount' for an individual can be for a higher amount than would otherwise apply. This rule will apply whether the structure of the arrangement concerned is to avoid the special annual allowance charge, the annual allowance charge, or the lifetime allowance charge.

5.3 When calculating the pension input amount for a defined benefits arrangement, for example, the amount to be determined is taken from the prospective entitlement to the scheme pension as at the commencement of the scheme pension. The annual allowance test is not concerned with the amounts of pension increases to be applied at a future date to a scheme pension in payment.

5.4 It is possible, therefore, that arrangements might be structured in such a way that the value of the increase in rights only in relation to the starting level of pension could be untypically low.

5.5 If a pension input amount under an arrangement is designed to be artificially low, the pension input amount must be calculated as the greater of

- the amount ordinarily calculated for the purpose of the current annual allowance, and which can otherwise also apply in relation to the special annual allowance and
- the amount found by taking the following opening value away from the following closing value
  - the opening value is
    - the amount that might be expected to be received by the individual if that individual member, or a dependant of the member, assigned the rights under the arrangement as they were at the start of the tax year concerned, and
  - the closing value is
    - the amount that might be expected to be received by the individual member, or a dependant of the member if that individual or dependent assigned the rights under the arrangement as they were at the end of the tax year concerned.

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

5.6 For the purpose of this calculation, it is to be assumed that the rights are freely assignable.

5.7 The rights under the arrangement for the purpose of the closing value must be adjusted, if necessary, in accordance with the same adjustments that would normally apply if considering the current annual allowance provisions. These are adjustments are to

- add to the closing value
  - any pension debit arising from a pension share on divorce or annulment during the tax year.
  - any amount of rights represented within a transfer of rights from the arrangement
  - any amount crystallised from a benefit crystallisation event in relation to the arrangement
- Subtract from the closing value
  - any pension credit acquired to the individual from a pension share on divorce or annulment
  - any rights representing a transfer of rights received by the arrangement
  - any minimum payments made relating to contracting-out rights

5.8 If an arrangement ceased to exist during a particular tax year the 'closing value' is taken to be the value immediately before the time at which the arrangement ceased to exist.

5.9 More details about these additions or subtractions can be found in the Registered Pension Schemes Manual, RPSM06103050 and RPSM06103060, which is available on the HMRC internet site at [ww.hmrc.gov.uk](http://www.hmrc.gov.uk).

### **Re-activated and new schemes**

5.10 The rule that allows contributions to schemes that are re-activated and newly set-up on or after 22 April 2009 to be protected pension inputs is set aside in some circumstances. This set aside applies only to occupational pension schemes or group personal pension schemes which relate to the employment of the individual where the provision of benefits is not part of the normal pattern of pension provision made by the employer in respect of its employees.

Indicators of normality are:

- It is one of a number of similar arrangements relating to employees of a specific employer or group of employers.
- Contributions are made to the arrangement on a regular basis (e.g. weekly or monthly) by the person's employer.

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

- There are more than 20 arrangements relating to active members who are employees of that employer or group of employers and the rules governing contributions are the same.
- It is set up in relation to a new employment for the individual who is accruing benefits.
- It is part of a scheme open to all employees of that employer on the same terms.
- The rules governing accrual of benefits that govern that arrangement are not restricted to a particular class of employees.
- If the rules are restricted to a particular class there have been no material alteration to those rules since 22 April 2009.
- The scheme is set up as part of a commercial reorganisation of the employer's pension schemes.

### **General Anti-avoidance rule for Protected Input Amounts**

5.11 An arrangement will cease to be an arrangement which creates protected pension input amounts if there are, in relation to that arrangement, a scheme or arrangement (or schemes or arrangements) which have as their main purpose or one of their main purposes to avoid liability to the special annual allowance charge, the current annual allowance charge or the lifetime allowance charge.

Note - the terms 'scheme' or 'arrangements' are used here in the sense of avoidance devices rather than pension schemes or pension arrangements. Such a 'scheme' or 'arrangement' includes any agreement, understanding, transaction or series of transactions (whether or not legally enforceable).

## Chapter 6 - £150,000 RELEVANT INCOME LIMIT

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6.1 The special annual allowance charge does not apply to everyone. It applies only to individuals with 'relevant income' of £150,000 or more. In practice this means individuals with:

- relevant income of £150,000 or more, and
- who have total adjusted pension input amounts in the 2009-2010 or 2010-2011 tax years.

6.2 The £150,000 relevant income limit for a tax year applies in respect of the amount of income that relates to the individual in that tax year, and in either of the previous two tax years. In practice, this means:

- for the 2009-2010 tax year
  - the special annual allowance will apply to individuals whose income is £150,000 or more in any of the 2007-2008, 2008-2009 or 2009-2010 tax years, and
  - who have adjusted pension input amounts for 2009-2010, and
- for the 2010-2011 tax year
  - the special annual allowance will apply to individuals whose income is £150,000 or more in any of the 2008-2009, 2009-2010 or 2010-2011 tax years, and
  - who have adjusted pension input amounts for 2010-2011.

### What is relevant income for the purpose of the £150,000 limit?

6.3 The 'relevant income' which needs to be taken into account for the purpose of the £150,000 income limit is arrived at after going through a step by step calculation before ending up with a figure to compare with the £150,000 or more figure.

#### Step 1 – total income

To start, take the total amounts of the individual's income that are within the charge to income tax for the tax year in question. This is the amount of income that is the figure at the first stage of section 23 Income Tax Act 2007.

This figure of total income includes

- earnings from employment
- earnings from self-employment/partnerships
- most pensions income (State, occupational and personal pensions)
- interest on most savings

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

- income from shares (dividend income)
- rental income, and
- income received by an individual from a trust.

However, it does not include amounts giving rise to income tax liabilities which are not treated as income for general tax purposes in connection with

- the recovery of excessive relief where the individual's self-assessment for the tax year is final (for example, the withdrawal or reduction of Enterprise Investment Scheme relief or the recovery of excess credit for overseas tax),
- deduction of tax at source where the liability is not in respect of the individual's own liability, and
- stand-alone tax charges (for example tax charges in respect of an unauthorised payment from a registered pension scheme)

The full list of amounts not included in the 'total amount of income' is in sections 30 and 32 of Income Tax Act 2007.

## **Step 2 - contributions to registered pension schemes under PAYE net pay arrangements and contributions under corresponding relief**

Add to the amount of the total income figure found in Step 1 the amount of any pension contributions made in the tax year under

- the net pay arrangement, or
- under the corresponding relief provisions in accordance with paragraph 51, Schedule 36 of the Finance Act 2004.

In particular, the net pay arrangement operates where the employer deducts contributions from the employment income before deducting any tax from that income under the PAYE payroll procedures within an occupational pension scheme or, where appropriate, public service pension schemes.

For the purpose of the £150,000 income limit, an individual's income in respect of a particular tax year includes amounts before any deductions are made under net pay arrangements. In other words, such contributions should be added to the total income of the individual as part of the steps to see whether the income limit is reached.

Member contributions to registered pension schemes which obtain tax relief by a method other than under net pay (such as under relief at source arrangements or on making a claim under the individual's self-assessment tax return) are made from taxed income and so are already included in the total income figure at Step 1. Therefore no adding in of such amounts is required.

More details about the corresponding relief provisions can be found in the Registered Pension Schemes Manual, RPSM13101100 onwards, which is available on the HMRC internet site at [www.hmrc.gov.uk](http://www.hmrc.gov.uk).

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. 29

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

### **Step 3 – certain losses and other reliefs**

Deduct from the figure after Step 2 amounts upon which the individual was entitled to tax relief for the tax year concerned and which arise under the list in section 24 of the Income Tax Act 2007. They are mainly concerned with deductions for trade and property losses, but do include some other items.

References in this list are also to the Income Tax Act 2007.

The list includes,

- Trade loss relief against general income (section 64)
- Carry-forward trade loss relief (section 83)
- Terminal trade loss relief (section 89)
- Post-cessation trade relief (section 96)
- Carry-forward property loss relief (section 118)
- Property loss relief against general income (section 120)
- Post-cessation property relief (section 125)
- Employment loss relief against general income (section 128)
- Share loss relief (Chapter 6 of Part 4)
- Loss relief against miscellaneous income (section 152)

Some types of loss relief can be deducted only from the kind of income that gave rise to the loss, and the amount the individual is entitled to for the year is therefore limited to the amount of that kind of income. For example, the individual has carry-forward trade losses of £5,000 for 2009-10 but their trading income for that year is £3,000. The individual is therefore entitled to carry-forward trade loss relief of £3,000 for the purposes of Step 3.

Note that tax relief on pension contributions under sections 193(4) or 194(1) of the Finance Act 2004 should not be deducted at this step.

### **Step 4 – relievable pension contributions**

From the amount found after Steps 1, 2 & 3, deduct the amount of any of the following:

- relievable pension contributions paid by, or on behalf of, the member during the tax year;
- any contributions in respect of which the individual is entitled to a tax reduction under section 788 of the Income and Corporation Taxes Act 1988 and.
- any contributions paid by the individual that qualify for relief under the corresponding relief provisions in accordance with paragraph 51, Schedule 36 of the Finance Act 2004.

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. 30

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

This is subject to a maximum deduction of £20,000. If an individual had relieviable contributions of more than £20,000 for the tax year the amount in excess of £20,000 cannot be deducted.

### **Step 5 - salary sacrifices**

Salary sacrifice is where an employee's employment income is reduced in exchange for the employer providing some other benefit. In this context, the employee's remuneration is reduced in exchange for a pension contribution by the employer. This step applies only if the salary sacrifice was agreed on or after 22 April 2009.

For the purpose of calculating the income of an individual to compare with the £150,000 or more limit, add back to the amount found after Step 4 any amount which has been agreed between the employee and the employer as being sacrificed in exchange for employer pension contributions.

For this purpose, 'a pension contribution by the employer' means an individual's employer, or some other person,

- agreeing to pay contributions (or additional contributions) to a pension scheme in respect of the individual, or
- agreeing to secure increased benefits under any pension scheme, whether by a contribution or by some other means, to which any of the following have an actual or prospective entitlement
  - the individual
  - a dependant of the individual, or
  - any person connected with the individual.

Section 993 of the Income Tax Act 2007 defines a 'connected person' for this purpose.

### **Step 6 – gift aid**

Deduct from the amount found after 'Step 6' the amount that represents any donations made in the tax year that qualify for 'gift aid' under Chapter 2 of Part 8 of the Income Tax Act 2007. This amount can also include amounts of qualifying donations that are treated as made in the same tax year under an election to carry back relief.

The amount found after Step 6 is the 'relevant income figure'.

If the amount is £150,000 or more, then the special annual allowance provisions will apply. If total adjusted pension input amounts exceed the individual's available special annual allowance, then the special annual allowance charge will apply.

#### **Example**

The calculation is for the 2009-2010 tax year

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. **31**

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

### Step 1

Mark's taxable employment income for the tax year 2009-2010 is £142,000 and other taxable income for the year of £20,000.

Mark's total income for the year is £162,000 (£142,000 + £20,000)

### Step 2

Mark's taxable employment income for the year would have been greater but for contributions of £9,000 that he made in the tax year to a registered pension scheme under the net pay arrangement.

The amount of those contributions is added to the 'Step 1' figure, giving an amount of £171,000 (£162,000 + £9,000)

### Step 3

Mark did not have any qualifying loss or other reliefs

The amount found after this step, therefore, is still £171,000

### Step 4

As well as the contributions of £9,000 under the net pay arrangement, Mark also made 'net' contributions of £10,000 to a personal pension scheme in the same year under the 'relief at source' arrangements. However, the total relievable contribution that Mark made for the year in respect of the personal pension scheme is the 'grossed up' amount of £12,500.

The total relievable contributions are £21,500 (£9,000 + £12,500) but only £20,000 can be deducted from the amount found at Step 3, giving an amount of £151,000 (£171,000 - £20,000)

### Step 5

No salary sacrifice arrangement was made in the tax year.

The amount found after this step, therefore, is still £151,000

### Step 6

Mark made a 'gift aid' qualifying donation of £500 in the tax year. This represents £625 (when the donation of £500 is grossed up), which is the amount deducted from the amount found at Step 5.

This gives an amount of £150,375 (£151,000 - £625), which is Mark's relevant income amount for the 2009-2010 tax year.

Mark's relevant income for 2010-2011 is £140,000 and in 2008-2009 it was £130,000. However, as Mark's relevant income amount for 2009-2010 was £151,375 this amount is Mark's relevant income amount for 2010-2011 also.

### **Anti-avoidance rule: relevant income**

6.4 Where an individual enters into a scheme or arrangement with the aim of reducing their relevant income below the £150,000 threshold, then the legislation assumes the relevant income to be £150,000. This rule would apply if the scheme was designed to affect any of the steps taken to arrive at relevant income, for example, by reducing income by moving some into another year or by turning it into capital, and by increasing deductions by using artificial losses etc.

Note - the terms 'scheme' or 'arrangements' are used here in the sense of avoidance devices rather than pension schemes or pension arrangements. Such a 'scheme' or 'arrangement' includes any agreement, understanding, transaction or series of transactions (whether or not legally enforceable).

## Chapter 7 - TOTAL ADJUSTED PENSION INPUT AMOUNTS

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7.1 For the special annual allowance charge to apply to an individual in relation to a particular tax year the following conditions must apply

- the individual has relevant income of £150,000 or more for that tax year or in either of the two years before the tax year in question
- for the tax year in question, the individual made pension savings and/ or pension savings were made in respect of the individual, and
- there has been a change to their pension savings that is over and above their 'normal ongoing pension savings'.

7.2 That amount over and above their normal ongoing pension savings is called the 'total adjusted pension input amount'.

7.3 If the total adjusted pension input amount for a tax year exceeds the special annual allowance for that tax year, the excess amount is subject to the special annual allowance charge.

7.4 The amount of the pension savings made by, or in respect of, an individual in a particular tax that needs to be tested against the special annual allowance as a total adjusted pension input amount is established in the following way:

### Step 1

The total amount of the pension savings by, or in respect of, the individual made during the tax year is valued, using the same method as is used to obtain a 'total pension input amount' for the purposes of the current annual allowance, except

- the input period is the tax year, and
- the circumstances in which the input amount is ignored are more limited.

### Step 2

From the amount representing what would be the 'total pension input amount' as calculated under the current annual allowance provisions as modified or under the pensions input amount anti-avoidance rule (see below), as the case may be, the following deductions can be made:

- a) the amount representing the total amount of protected pension input amounts for the individual for the tax year in question;
- b) the amount representing the total amount of any refund lump sums made in respect of the individual for the tax year in question; and
- c) (for the 2009-2010 tax year only) the amount representing that part of the 'total pension input amount' found under the current annual allowance provisions as modified that relates to the period beginning on 6 April 2009 and ending on 21 April 2009.

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. **34**

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

### Step 3

If there is any amount of 'total pension input amount' left after any of the deductions that residual amount or, if there are no deductions, the whole of the 'total pension input amount' is the adjusted pension input amount for the purposes of the special annual allowance.

### Step 6

If the total adjusted pension input amount for a tax year exceeds the special annual allowance for that tax year, the excess amount is subject to the special annual allowance charge unless there is an adjustment because the individual also happens to be liable to the current annual allowance charge in the same tax year.

#### Example

John has a defined benefits arrangement. He is drawing a salary of £150,000 each year. Since he joined the pension scheme in 1995 he has been accruing rights using an accrual rate of one-sixtieth of salary for each year of service. He is not a member of any other scheme.

His current annual allowance test is based on pension input periods which end on 5 July, which is the end-date of the scheme year used for all the members of the scheme. From 6 July 2009, the rules of the pension scheme are changed. The accrual rate is increased from 60ths to 30ths and all pensionable service counts for the purpose of the calculation of the increased rate of accrual. John is one of only 4 members who are subject to this provision.

#### Step 1:

Value of savings at 5 April 2010 is  $14.75/30\text{ths}$  of £150,000 = £73,750 multiplied by 10 = £737,500.

Value of savings at 6 April 2009 is  $13.75/60\text{ths}$  of £150,000 = £34,375 multiplied by 10 = £343,750.

The increase in the value of his savings in 2009-2010 is £737,500 - £343,750 = £393,750 (total pension input amount).

#### Step 2:

(a) Work out the protected pension input - which is the change in value of savings in the tax year, ignoring the 6 July 2009 change in defined benefit accruals.

Value of savings at 5 April 2010 would have been  $14.75/60\text{ths}$  of £150,000 = £36,875 multiplied by 10 = £368,750.

Value of savings at 6 April 2009 is  $13.75/60\text{ths}$  of £150,000 = £34,375 multiplied by 10 = £343,750.

The increase in the value of his savings in 2009-2010 would have been £368,750 - £343,750 = £25,000.

(b) No refunds made

(c) Work out the amount of the total pension input amount that relates to 6 to 21 April 2009 – which is  $16/365 \times £393,750 = £17,260$

(a)+(b)+(c) = £42,260

Deduct (a)+(b)+(c) from total pension input amount to give:

Step 3: Adjusted pension input amount =  $£393,750 - £42,260 = £351,490$

Step 4: Special annual allowance is £20,000 less the protected pension input at (a) to a maximum of £20,000 = nil

Amount subject to special annual allowance charge is £351,490

The special annual allowance charge will be 20% of £351,490 = £70,298.

7.5 How pension input amounts are established for the purpose of establishing the 'total pension input amount' under the provisions for the current annual allowance, as modified, in order to establish a total adjusted pension input amount for the purpose of the special annual allowance will depend on the type of arrangement under which an individual's pension saving in is made.

7.6 The basic principles for how to calculate pension input amounts are described below. Full details about each calculation can be found in the Registered Pension Schemes Manual, RPSM06100000 onwards, which is available on the HMRC internet site at [www.hmrc.gov.uk](http://www.hmrc.gov.uk). Though these details must be applied on the basis that the pension input amount is that for the tax year question for the purpose of the special annual and the pension input period is that same tax year.

### **Anti-avoidance rule**

7.7 If an input amount is subject to the total pension input amount anti-avoidance rule the input amount is the greater of:

- the amount established as the 'total pension input amount' established by reference to the current annual allowance provisions as modified, and
- the amount established under this anti-avoidance rule.

### **Input amounts – 'other' money purchase arrangements**

7.8 The pension input amount in respect of a money purchase arrangement other than a cash balance arrangement is the total of:

- any tax relievable pension contributions paid by or on behalf of the individual under the arrangement, and
- contributions paid in respect of the individual under the arrangement by an employer of the individual,

during the tax year.

## Defined benefit arrangements

7.9 In a defined benefits arrangement, the pension input amount is the amount of any increase in the value of the individual's rights under the arrangement during the tax year.

7.10 For this purpose, a comparison is made between the value of the individual's rights under the arrangement at the beginning of the tax year and the value of those rights at the end of the tax year. There will be an increase in the value of the individual's rights under the arrangement during the tax year if

- the value of the individual's rights under the arrangement at the beginning of the tax year (the "opening value") is less than
- the value of the individual's rights under the arrangement at the end of the tax year (the "closing value").

## Cash balance arrangements

7.11 For cash balance arrangements the pension input amount is the amount by which an individual's rights under the arrangement have increased over the tax year. There is such an increase when the closing value of an individual's rights exceeds the opening value.

7.12 Both the opening value and the closing value of the individual's rights are the amounts that would be available for the provision of benefits to or in respect of the individual on the assumption that the individual became entitled to them on the calculation dates specified, i.e. the beginning and end of the tax year. For this purpose, it is assumed that the rights under the arrangement are not affected by any scheme provision to discount pension rights by an actuarial reduction for early payment and that any calculation of rights for ill- health under the scheme provisions are ignored.

## Hybrid arrangements

7.13 A hybrid arrangement is one where the benefits are calculated as one of two or three alternatives, for example, a defined benefits and money purchase. In these circumstances it is impossible to establish the character of the pension benefit that will ultimately be paid until it is actually paid. Consequently the pension input amount must be calculated on the basis that the pension will be provided by each of the types of benefit that may be payable under the arrangement (cash balance benefits, other money purchase benefits, or defined benefits as appropriate) and then using the greater or greatest of these amounts as the final figure.

7.14 Scheme administrators and members do not have to unwind current pension input periods that are in place in relation to the current annual allowance as they will continue to apply in the usual way.

7.15 The special annual allowance applies only to adjusted pension input amounts that occur in the tax years 2009-2010 and after. Pension input amounts made during the 2009-2010 and later tax years that have been measured for the purpose of

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

establishing a total adjusted pension input amount are also be measured, in the usual way, for the purpose of the current annual allowance..

#### Example

At 22 April 2009 Mark is accruing benefits under a defined benefits scheme. Mark has no other rights accruing under this or any other pension scheme.

The pension input period for the purpose of the current annual allowance that was running at 22 April 2009 commenced on 2 June 2008 and ended on 1 June 2009.

On 1 June 2008 Mark had completed 10 years pensionable service and his pension benefit accrued at  $1/60^{\text{th}}$  of salary for each year of service. His pensionable salary was £180,000. Accordingly his pensionable entitlement on that date was £30,000 ( $10 \times 1/60^{\text{th}} \times £180,000$ ). A lump sum is available only by commutation of pension.

By 1 June 2009 Mark's pensionable salary had risen to £185,000. Accordingly his pensionable entitlement on that date was £33,917 ( $11 \times 1/60^{\text{th}} \times £185,000$ ).

The increase in Mark's pension rights under this arrangement was therefore £39,170 ( $(£33,917 \times 10) - £30,000 \times 10$ ).

As there had been no change to the basis on which Mark's benefit rights had accrued between 22 April 2009 and 1 June 2009 the increase in Mark's benefit rights is a protected pension input amount for the purpose of the current annual allowance. (The input amount is within the current annual allowance of £245,000 for 2009-2010 and so Mark had no annual allowance charge to pay in respect of the input.)

At the end of the 2009-2010 tax year Mark is still accruing benefits under the same defined benefits scheme and on the basis ( $1/60^{\text{th}}$  of salary for each year of service) and during 2009-2010 Mark had no other rights under this or any other pension scheme. Mark, therefore, did not have any adjusted pension input amounts for the purpose of the special annual allowance pension input period for 2009-2010.

### **What about the period between the start of the 2009-2010 tax year and 22 April 2009?**

7.16 Any increases in pension saving made between 6 April 2009 and 21 April 2009 will be protected amounts.

7.17 This means that any contributions paid to other money purchase schemes on or after 6 April 2006 and before 22 April 2009 will not be tested against the special annual allowance.

7.18 For cash balance and defined benefits schemes it is the proportion of the pension input amount that relates to the period from on or after 6 April 2009 to immediately before 22 April 2009.

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. **38**

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

7.19 For hybrid arrangements it is determined by reference how the benefits accrued for the arrangement in question over the pension input period. For example, if greatest amount by which the benefits accrued was on an 'other' money purchase basis then any contributions paid on or after 6 April 2006 and before 22 April 2009 will not count for the purpose of the special annual allowance.

## Chapter 8 - BECOMING ENTITLED TO BENEFITS UNDER AN ARRANGEMENT

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8.1 For the purposes of the special annual allowance where all benefits are taken under an arrangement, there will, except as provided below, be a test against the available special annual allowance. This is different from the position of the current annual allowance.

8.2 The special annual allowance test will not apply in respect of an arrangement where, before the end of the tax year the individual has become entitled to all of the benefits from the arrangement in either Condition A or Condition B applies: . These are:

### Condition A

- the member's arrangement is a defined benefits arrangement and, at the time that the benefits are taken, there are at least 20 members in the pension scheme

and

- that the taking of benefits is not part of a scheme or arrangement the main purpose, or one of the main purposes, is to avoid the special annual allowance charge

### Condition B

- the benefits are being paid because the individual meets the 'ill-health condition' and the arrangement is held under any of the following pension schemes
  - an occupational pension scheme
  - a public service pension scheme, or
  - a group personal pension scheme.

8.3 In the event of the death of the member in the tax year concerned, or the payment of a serious ill-health lump sum under the arrangement, no test will apply for the purpose of the current annual allowance, as is already the case, but a test against available special annual allowance will apply.

### Example

Linda has a money purchase arrangement with a fund to which she has not made any contributions since 2005. On 1 July 2009 she pays a contribution of £300,000 and on 1 August 2009 she has arranged with the scheme to draw a pension commencement lump sum and designates the remainder of the fund as available to pay an unsecured pension.

There will be a test against the special annual allowance.

The amount of £300,000 gives rise to an adjusted pension input amount of £300,000, and there is no protected pension input amount to deduct. The special annual allowance in this instance is £20,000. The amount chargeable to the special annual allowance charge is therefore £280,000.

Linda will be liable to a special annual allowance charge of 20% of £280,000 = £56,000.

Note that there is no test against the current annual allowance in this case (because it is set aside for the tax year in which all benefits are taken), despite the pension input amount exceeding the current annual allowance. The difference is because the special annual allowance rule about setting aside the test for the tax year of taking benefits is more limited.

## Chapter 9 - SPECIAL ANNUAL ALLOWANCE TAX CHARGE

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9.1 When the special annual allowance is exceeded there is an income tax charge called the 'special annual allowance charge'.

9.2 The special annual allowance charge is a tax charge on the individual.

9.3 It arises where the total adjusted pension input amount for an individual for that tax year exceeds the amount of the available special annual allowance for that tax year for that individual. The first year it will apply is 2009-2010.

9.4 Where the total adjusted pension input amount exceeds the special annual allowance, the special annual allowance charge is levied on the excess.

9.5 The special annual allowance charge is to recover the excess of relief at tax rates higher than basic rate. Basic rate tax relief effectively continues.

9.6 For 2009-2010, the special annual allowance charge is set at 20% and is charged on the excess of the special annual allowance.

9.7 However, if an individual ever became liable to both the special annual allowance charge and the current annual allowance charge there will be a reduction to the amount subject to the special annual allowance charge to prevent double-charging.

## Chapter 10 - INTERACTION WITH THE CURRENT ANNUAL ALLOWANCE

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10.1 The special annual allowance runs alongside the current annual allowance that was introduced from the tax year 2006-2007 onwards. Both annual allowances will apply from 2009-2010. However, the special annual allowance will apply only in respect of individuals who have relevant income of £150,000 or more.

10.2 It is possible for an individual to be subject to an annual allowance tax charge under the current annual allowance but not be subject to the special annual allowance charge.

### Example

On 1 June 2008 Mark started a pensionable employment with a starting annual salary of £730,000. Mark's pensionable service with that employer also started on 1 June 2008 and his pension benefits accrue on a 1/30th accrual rate and a lump sum is available only by commutation of pension.

Mark has no other rights accruing under this or any other pension scheme.

For the purpose of the current annual allowance Mark's first pension input period in respect of his defined benefit arrangement started on 1 June 2008.

By 1 June 2009, the end of the first pension input period for the purpose of the current annual allowance, Mark's pensionable entitlement was £24,333 (1 x 1/30th x £730,000).

The increase in Mark's pension rights under this arrangement was, therefore, £243,330 ((£24,333 x 10) (the opening value of the benefits under the arrangement was nil).

By 1 June 2010, the end of the second pension input period for the purpose of the current annual allowance, Mark's pensionable salary had risen to £766,500. Accordingly his pensionable entitlement on that date was £51,100 (2 x 1/30th x £766,500). The increase in Mark's pension rights under the arrangement was, therefore, £267,670 ((£51,100 x 10) - £24,333 x 10)).

For the purpose of the special annual allowance, the increase in Mark's pension rights are in accordance with the terms of the employment contract that Mark had in place with his employer immediately before 22 April 2009. The pension input amounts of £243,330 (no charge under the current annual allowance) and £267,670 (charged under the current annual allowance) are, therefore, protected pension input amounts and so the special annual allowance does not apply to either of those input amounts.

For the purposes of the current annual allowance, the £243,330 increase in Mark's pension rights for the pension input period ending in the tax year 2009-2010 was within the current annual allowance of £245,000 for that year. Mark has no annual allowance charge to pay in respect of the current annual allowance for that year.

However, the £267,670 increase in Mark's pension rights for the pension input period ending in the tax year 2010-2011 was in excess of the current annual

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

allowance of £255,000 for that year. He will therefore be liable to an annual allowance charge in respect of the excess amount.

10.3 Alternatively, it is possible for an individual to be subject to an annual allowance tax charge under the current annual allowance and be subject to the special annual allowance charge under the special annual allowance.

10.4 When an individual is subject to a tax charge under both the current annual allowance and the special annual allowance an adjustment is made to the amount subject to the special annual allowance charge.

10.5 Ordinarily, the special annual allowance charge applies in respect of the amount by which an individual's total adjusted pension input amount exceeds the individual's special annual allowance.

#### Example

Mark's special annual allowance is £20,000 and Mark has a total adjusted pension input amount of £25,000. The special annual allowance charge will apply in respect of the excess amount of £5,000 (£25,000 - £20,000).

10.6 Where an individual is liable to the annual allowance charge in respect of the current annual allowance as well, there will be an excess amount in relation the individual's total pension input amounts that have been determined, in the usual way, for the purpose of the current annual allowance. The amount representing the excess on the annual allowance is deducted from the excess amount that has been determined for the purpose of the special annual allowance.

#### Example

Mark has relevant income for 2009-2010 of £150,000.

Mark pays a contribution of £295,000 into an 'other' money purchase arrangement in May 2009 in a pension input period that ends on 1 June 2009 for the purpose of the current annual allowance. The current annual allowance for 2009-2010 has been exceeded by £50,000 (£295,000 - £245,000). Mark is liable for current annual charge of £20,000 (£50,000 x 40%).

The contribution of £295,000 is the only pension savings that Mark makes in 2009-2010 and the amount is not a protected pension input amount.

Mark is also liable to the special annual allowance charge in respect of the same contribution as that contribution also exceeded Mark's special annual allowance for 2009-2010 of £20,000.

Amount that would ordinarily be subject to the special annual allowance charge is £275,000 (£295,000 - £20,000). However, as Mark is also liable to the current annual allowance in 2009-2010 the amount ordinarily subject to the special annual charge (£275,000) is reduced by the amount of the excess that is subject to the current annual allowance charge (£50,000).

Mark is liable to the special annual allowance charge of £45,000 ((£275,000 - £50,000) x 20%).

## Chapter 11 - REFUNDS OF CONTRIBUTIONS

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11.1 The special annual allowance is introduced with immediate effect from 22 April 2009. It is possible, therefore, that individuals with taxable income of £150,000 or more might make pension scheme contributions in 2009-2010 or later without realising that they will be subject to special annual allowance charge because that pension saving is an adjusted pension input amount that has exceeded the available special annual allowance.

11.2 The rules on refunds mean that where a refund of contributions meets certain conditions, it is deducted from the total adjusted pension input amount for the year the contributions were paid. The amount of the refund (the contributions refund lump sum) will not therefore be subject to the special annual allowance tax charge. The refund will not be treated as an unauthorised payment.

11.3 A refund of contributions is a 'contributions refund lump sum' if it meets the following conditions:

- it relates to a particular arrangement under the pension scheme. This must be either in relation to a scheme that is not an occupational pension scheme or to an AVC,
- the contribution does not relate to protected pension arrangements,
- the person making the contributions was a high-income individual in the tax year the contributions were made (i.e. their relevant income was £150,000 or more for the tax year or in either of the preceding two tax years, or both),
- the refund lump sum relates to contributions paid by an individual in a particular tax year which is not earlier than the 2009-2010 tax year
- the refund lump sum is paid in the tax year following the tax year to which the refund relates (i.e. if the refund relates to contributions paid in 2009-2010, the payment must be made in 2010-2011),
- the refund lump sum is not any of the lump sums<sup>1</sup> in section 166(1) Finance Act 2004
- the amount of the refund does not exceed the amount of the contributions paid by the individual under the arrangement in the tax year in question less any amounts representing the following

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<sup>1</sup> The lump sums list in section 166(1) Finance Act 2004 are:

- a pension commencement lump sum
- a serious ill-health lump sum
- a short service refund lump sum
- a refund of excess contributions lump sum
- a trivial commutation lump sum
- a winding-up lump sum, or
- a lifetime allowance excess lump sum

- contributions paid by the individual on or after reaching age 75
- contributions which are life assurance premium contributions
- any previous refund lump sum paid in the same tax year in respect of the arrangement
- any pension debit applied to the individual's rights under the arrangement where that debit was applied in the same tax year to which the refund lump sum relates
- the sums or market value of assets transferred out of the arrangement in respect to the individual to another registered pension scheme or qualifying recognised overseas pension scheme in the tax year to which the refund lump sum relates
- any benefit crystallisation event that occurred in relation to the individual and the arrangement in the tax year to which the refund relates, and
- for the purpose of the 2009-2010 tax year, any contributions paid on or after 6 April 2009 but before 22 April 2009.

11.4 More details about the lump sums, life assurance premium contributions, transfers and benefits crystallisation events mentioned above can be found in the Registered Pension Schemes Manual, which available on the HMRC internet site at [www.hmrc.gov.uk](http://www.hmrc.gov.uk).

11.5 Contributions made by an employer of the member are not to be included within any refunded lump sum.

11.6 The amount refunded must represent the total amount of the 'gross contribution' that has been made by, or on behalf of, the individual. This means that individual for whom a 'net contribution' was paid under the 'relief at source' arrangements should receive a payment that represents both the 'net amount' paid and the 'top-up' relating to the basic rate tax relief given in respect of the contribution.

11.7 The relief at source claim as made by the provider of the pension scheme in respect of a contribution that is then refunded in this way must not be later altered as a result of the payment by the scheme of the refunded amount.

11.8 A tax charge will apply in respect of such a payment of a refund. The tax charge will be at a rate of 40% of the amount of the payment made to the individual. The tax charge is the scheme administrator's liability. The individual is not liable to this tax charge.

11.9 If a payment is made and the scheme administrator accounts for the tax charge due by way of a deduction from the 'gross amount' of payment that would otherwise have been paid, the tax charge is based on that 'gross' amount.

#### Example

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An individual is due to receive a payment of £30,000 from a pension scheme representing a corresponding amount of contributions that the individual paid to that scheme in the tax year 2009-2010.

The scheme administrator's tax liability is £12,000 (£30,000 x 40%).

The scheme administrator account for the tax due by making a deduction from the payment the individual would otherwise have received and so the individual receives a payment of £18,000 (£30,000 - £12,000).

11.10 The amount of the payment in respect of a particular arrangement cannot exceed the amount of the contributions paid by the individual under that arrangement in the particular tax year for it to be an authorised member payment. In effect, this only allows the individual to get back his or her own contributions. The payment does not allow for any employer contributions paid in respect of the individual or any other contributions paid on behalf of the individual to be returned to the individual.

11.11 The scheme administrator must account for the tax due in respect of such a payment in the same way that the scheme administrator might account for tax charges it might be liable for in respect of a registered pension scheme (other than the scheme sanction charge). The scheme administrator is required to make an 'Accounting for Tax Return' in respect of any tax the administrator has become liable in any designated 3-month period. The 3-month periods are the quarters ending 31 March, 30 June, 30 September and 31 December.

11.12 An 'Accounting for Tax Return' is in electronic format for this purpose and is available on the HMRC internet site, by going to 'Pension Schemes Online'. The completed form must be delivered to HMRC electronically within 45 days beginning with the day immediately following the end of the relevant 3-month period. A practitioner can submit the Accounting for Tax Return if authorised by the scheme administrator to do so.

11.13 The income tax in respect of which the return is made must be paid within the same time limit as is given for completion of the return, that is within 45 days following the end of the 3-month period. It is payable without the making of an assessment by HMRC. For more details about how to make the payment, please see the separate guidance on the HMRC website, by going to the homepage at [www.hmrc.gov.uk](http://www.hmrc.gov.uk) and following the links for 'How to pay' to find the instructions for a pension scheme.

11.14 However, for refunds of 2009-2010 contributions, there will be no bespoke arrangements under the 'Accounting for Tax Return' for the paying the tax charge due in respect of these particular payments. Instead, we will be asking the scheme administrator to use existing boxes for accounting for tax in respect of a short service refund.

11.15 Ideally we would ask scheme administrators to put the full amount of any refunds in the '40% box' for the short service refund procedure. However, the return capture process will not accept an entry in the '40% box' unless there is a non-zero entry in the '20% box'. So if the scheme administrator has no short service refunds less than £10,800, we will be asking scheme administrators to put an amount of £1 in the '20% box' of the short service refund procedure and the balance amount of the payment in the '40% box'.

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

### Example

For a refund payment of £30,000, £1 is put in the '20% box' and £29,999 is put in the '40% box'.

11.16 In practice, the first time an 'Accounting for Tax Return' in respect of such a refund will be submitted is after the end of the 2009-2010 tax year.

11.17 Any payments back to an employer would have to meet the conditions of an authorised member or employer payment, as the case may be. For example, a refund to the employer from an occupational pension scheme would have to meet the conditions of an authorised surplus payment for it to be an authorised employer payment. A payment to the employer from a pension scheme that is not an occupational pension scheme or a public service pension scheme would be an unauthorised member payment.

11.18 The tax rules do not give a statutory right to such a refund. Instead it is a matter for those involved with the management of the pension scheme to decide if they can make arrangements for such refunds.

## Chapter 12 - OVERSEAS PENSION SCHEMES

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12.1 The legislation for the special annual allowance includes provision enabling extension of the rules on special annual allowance to be applied to members of currently-relieved non-UK scheme. But this is dependent on a Treasury Order setting out the conditions.

12.2 A pension scheme is a currently-relieved non-UK pension scheme in relation to a tax year if it is not a registered pension scheme and if one or both of the following conditions is met:

- relief from UK tax is given in respect of individual or employer contributions paid to it during the tax year by virtue of Schedule 33 of Finance Act 2004 or under double tax arrangements. That includes contributions that have received migrant member relief and employer contributions in respect of which an employee is tax-exempt under section 308A Income Tax (Employment and Pensions) Act 2003 (ITEPA).
- It also includes contributions that have received transitional corresponding relief under paragraph 51 of Schedule 36 of Finance Act 2004, or under article 15 or 17 of The Taxation of Pension Schemes (Transitional Provisions) Order 2006. The contributions must have been made after 5 April 2006.
- any of its members has been exempt from liability to tax by virtue of section 307 ITEPA in respect of provision for retirement or death benefits made by their employer at any time during the tax year when it is an overseas pension scheme. Provision must have been made after 5 April 2006.

12.3 A pension scheme is an overseas pension scheme if it is not a registered pension scheme but it is established in a country or territory outside the UK and satisfies the requirements in the Pension Schemes (Categories of Country and Requirements for Overseas Pension Schemes and Recognised Overseas Schemes) Regulations 2006 [SI2006/No 206].

12.4 More details about currently-relieved non-UK pension schemes can be found in the Registered Pension Schemes Manual, RPSM13102300 onwards, which is available on the HMRC internet site at [www.hmrc.gov.uk](http://www.hmrc.gov.uk).

## Chapter 13 - DEFINITIONS

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13.1 This guidance uses a number of defined terms some of which are used generally for the purposes of the tax rules for registered pension schemes. Some of these terms are explained below. More details about most of the terms listed below can be found in the Registered Pension Schemes Manual, which is available on the HMRC internet site at [www.hmrc.gov.uk](http://www.hmrc.gov.uk).

### **What is an active member?**

An individual in a defined benefits or cash balance arrangement is an active member if they have benefits currently accruing, or in an other money purchase arrangement who is currently making contributions or has contributions being made in respect of that individual.

### **What is an arrangement?**

A contractual or trust-based arrangement made by or on behalf of a member of a pension scheme under that scheme. A member may have more than one arrangement under a scheme.

### **What is a cash balance arrangement?**

An arrangement is a cash balance arrangement where the member will be provided with money purchase benefits, but where the amount that will be available to provide those benefits is not calculated purely by reference to payments made under the arrangement by or on behalf of the member. This means that in a cash balance arrangement, the capital amount available to provide benefits (the member's "pot") will not derive wholly from any actual contributions (or credits or transfers) made year on year.

For example, the scheme may promise that on retirement, a specified amount will be made available to provide the member with benefits for each year of pensionable service. The specified amount might be an absolute amount, e.g. £5,000 per year of service, or might be a percentage of the member's salary for each relevant year of service. Optionally, the scheme might also guarantee a rate of investment return on the specified amount. The member knows what will go into the promised pot each year (regardless of any contributions actually made) and so can ascertain the amount that accrues in that promised pot each year. It is possible that in a cash balance arrangement the promised pot builds up entirely notionally year by year, being funded only at the end. So, during the build-up phase, the amount in any actual fund held in respect of the member (whether more or less than the amount in the promised pot) is irrelevant. And when benefits ultimately become due, the amount in the promised pot is funded and it is that amount that is used to provide benefits.

In a cash balance arrangement, some of the investment and mortality risk is transferred to the scheme (or, if there is one, the employer); the fact that all or part of the pot is guaranteed or promised means that the promised amount must be made available to provide benefits irrespective of the level of actual funds held.

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

### **What is a defined benefits arrangement?**

An arrangement other than a money purchase arrangement that provides only defined benefits.

“Defined benefits” are calculated by reference to the earnings or the service of the member, or by any other means except by reference to an available amount for the provision of benefits to or in respect of the member, (thus making the definitions of money purchase and defined benefit arrangements mutually exclusive).

A defined benefit arrangement is, typically, a ‘final salary’ scheme, that is, one where the level of benefits paid is calculated by reference to the member’s final salary and length of service with the employer. Contributions are often made to such an arrangement, and so there may be a pension fund or pot, but the benefits that may be paid are not calculated by reference to that fund or pot.

### **What is a money purchase arrangement?**

An arrangement is a money purchase arrangement if, at that time, all the benefits that may be provided to or in respect of the member under the arrangement are cash balance or other money purchase benefits.

### **What is an ‘other’ money purchase arrangement?**

An arrangement is an ‘other’ money purchase arrangement where the member will be provided with money purchase benefits, and the amount that will be available to provide those benefits is calculated purely by reference to payments made under the arrangement by or on behalf of the member. This means that in an other money purchase arrangement the capital amount available to provide benefits (the member’s “pot”) will derive wholly from actual contributions (or credits or transfers) made year on year.

The scheme administrator or trustees may use the payments made under the arrangement to make investments of any kind on behalf of the member (for example, cash on deposit, shares, other investment assets, a life assurance policy on the member’s death). As long as the pot ultimately used to provide benefits is wholly derived from the original payments, the arrangement is an other money purchase arrangement. The subsequent investment income and any capital gains are derived from payments made under the arrangement, and they themselves become part of the member’s pot.

It is a feature of other money purchase arrangements that the member bears all the investment and mortality risk. The scheme simply pays out whatever benefits the amount in the pot, including the proceeds of all the investments that have been made using the payments into the scheme, will support.

### **What is a relievable pension contribution?**

A relievable pension contribution is a contribution by, or on behalf of, a member of a registered pension scheme and which is potentially capable of attracting tax relief. But amounts paid after the member has reached age 75, life assurance premium

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contributions, minimum contributions for contracting out purposes or amounts paid by an employer are not relivable pension contributions.

### **What is the 'ill-health condition'?**

An individual qualifies for the 'ill-health condition' where the scheme administrator accepts qualified medical advice to the effect that the individual is, and will continue to be, medically incapable (either physically or mentally), as a result of

- injury,
- sickness,
- disease, or
- disability,

of continuing his or her current occupation and as a result of the ill-health ceases to carry on the occupation.

### **What is an occupational pension scheme?**

A pension scheme is an occupational pension scheme if the scheme established by an employer or employers and having (or capable of having) effect so as to provide benefits to or in respect of any or all of the employees of that employer or employers, or any other employer (whether or not it also has effect so as to provide benefits to or in respect of other persons, or is capable of having such effect).

### **What is a public service pension scheme?**

A pension scheme is a public service pension scheme if the scheme is

- established by or under any enactment,
- approved by a relevant governmental or Parliamentary person or body, or
- specified as being a public service pension scheme by a Treasury order.

### **What is group personal pension scheme?**

Arrangements administered on a group basis under a personal pension scheme which are available to employees of the same employer or of employers which are in the same group of companies.

For this purpose a 'group' is formed by a company and all of its '75% subsidiaries' If any of those '75% subsidiaries' have '75% subsidiaries' the group includes them and their '75% subsidiaries' and so on. '75% subsidiary' is defined in section 838 of the Income and Corporation Taxes Act 1988.

### **What is a personal pension scheme?**

A pension scheme that is neither an occupational pension scheme nor a public service pension scheme