# Pensions Update No 150

29th March 2005

Please pass a copy of this Update to everyone in your organisation who needs to see it. The category of schemes covered by this Update is shown below. Italicised terms are explained in the glossary at the end.

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| **Category:** | All approved pension schemes. |
| **Action:** | For information only. |
| **Current Position:** | The Inland Revenue limits how much pension and lump sum may be paid by occupational pension schemes. These limits will be removed on 6th April 2006. This change may generate some tax-planning. |
| **Summary:** | As we move towards the 6th April 2006 changes, the Inland Revenue will address schemes or arrangements that exploit unintended features of the current regime, particularly where this is done so as to obtain advantages that are unintended in the new system. |
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## U 150: Pre A-Day Avoidance

### Section 590 Schemes

1. There are a number of sections of legislation that enable tax-advantaged retirement benefit provision. Most customers will be familiar with 'discretionary approval' for occupational schemes under *s591 ICTA'88*. However there is also a less used mandatory route to approval for occupational schemes via *s590* of the same Act.

2. The limits that apply to pensions and lump sums paid from *s591* approved schemes are specified under discretionary powers given to the Inland Revenue by the legislation. These limits are published in *PN*. Such a discretionary approach allows the Inland Revenue to respond to case-by-case considerations.

3. By contrast, the limits that apply to *s590* schemes, are set out in the legislation itself. The Inland Revenue has become aware of growing interest in *s590* schemes. On occasions, this may amount to an unintended use of the legal provisions of *s590* to get around in unacceptable ways benefit limits placed on *s591* schemes.

### An example of abuse

5. The Inland Revenue has recently been made aware of a possible method of quickly double-funding substantial retirement benefits in the run-up to *A-day*.

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6. A director with long service with his company, opts out of pensionable service and transfers his maximum accrued benefits under a *s591* approved scheme out to a personal pension scheme. The *s591* scheme then winds up and a *s590* scheme is set up to provide additional benefits, back-funded for the years which had already been fully funded in the *s591* scheme. The effect of this is to get around the benefit limits applying to occupational schemes approved under discretionary practice in an artificial way.

7. The Inland Revenue are likely to view this type of staged and exploitative activity as a scheme or arrangement leading to tax avoidance which started at the point of transfer out of the *s591* scheme. When such abuses come to light this will call into question the approval of the originating *s591* scheme.

## Transition

8. As we move towards the new simplified pensions regime which takes effect on *A-Day*, the example of abuse outlined above takes on an extra degree of urgency, as it could potentially boost a person's *personal lifetime allowance* for *protection* purposes.

10. Transitional *protection* for pre *A-day* rights is only intended to apply to amounts legitimately built up under the current regime. There is no objection to people legitimately maximising their benefits in the run-up to *A-day* where they are able to do so. But such efforts should remain within the bound of the published discretionary practice as outlined in *PN*. As explained above, where schemes or arrangements which seek to circumvent the limitations in PN come to light, the Inland Revenue will consider whether this affects the approval of the schemes involved. This applies whether or not the scheme or arrangement is more or less similar to the example above.

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## Glossary

**A-Day** - 6th April 2006 (contained in section 284(1) FA 2004).

**ICTA'88** - Income and Corporation Taxes Act 1988

**Personal Lifetime Allowance** – The lifetime allowance is a limit on the amount of tax privileged funds that an individual may accumulate under registered pension schemes after *A-day*. If this limit is exceeded, the excess becomes subject to a recovery tax charge. A personal lifetime allowance is the amount of an individual's pre *A-day* rights registered with the Inland Revenue for *protection* from the imposition of a lifetime allowance recovery charge.

**PN** - Practice Notes (IR 12). An Inland Revenue guide on the approval of occupational pension schemes, available on: www.inlandrevenue.gov.uk/pensionschemes/guidance.htm'.

**Protection** - Protection is a way of preserving the capital value of pre-*A-day* benefits which would otherwise be above the level of the lifetime allowance, from the imposition of a lifetime allowance recovery charge.

**s590** - Section 590 of *ICTA'88*.

**s591** - Section 591 of *ICTA'88*.