MEETING	**Pensions Committee**
DATE	**3 December 2010**
TITLE	**Restricting tax relief on pension savings**
PURPOSE FOR THE REPORT	**For Information**
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RECOMMENDATION	**To note the content**

1. INTRODUCTION

1.1 Included in the June 2010 budget was government confirmation of their commitment to restrict tax relief on annual and life time pension scheme accrual in a way that was "To ensure that the system of pensions tax relief remains fair and sustainable, and to protect the public finances."

1.2 The Government states that it provides generous tax relief to save for a pension encouraging individuals to take responsibility for retirement planning and in recognizing that pensions are less flexible than other forms of saving. The cost of pension tax relief net of income tax was around £19bn in 2008-09.

2. SUMMARY OF THE NEW PENSIONS TAX REGIME

2.1 From April 2011 the Annual Allowance (AA) for tax-privileged saving will be reduced from its current level of £255,000 to £50,000. Tax relief will be available at the individual's marginal rate.

2.2 Deemed contributions to defined benefit (DB) schemes are to be valued using a "flat factor" of 16 with individuals being allowed to offset contributions exceeding the annual allowance against unused allowance from the previous three years.

2.3 The Government sought the Government Actuary's advice on the appropriate level of the factor and decided to set the level at 16 – meaning, broadly, that an increase in annual pension benefit of £1,000 would be deemed to be worth £16,000. Previous year's benefits would be revalued against the CPI index with any negative accruals being treated as zero.

2.4 The Government will consult on options that enables individuals who see a very significant increase in their pension rights in a specific year to pay the tax charge out of their pension rather than current income.

2.5 It has been decided that deferred members will be excluded from the regime.

2.6 The Government believes that the restriction of pensions tax relief must apply fairly to individuals in different circumstances as far as possible, but that it must also be robust against risks of avoidance.

2.7 It is also made clear that it is not appropriate to apply the AA test in the year of death or the year in which lump sums are paid where individuals are diagnosed with serious (terminal) ill health.

2.8 The Government also recognizes that in some cases of major ill health it would be inappropriate for the AA to apply and will also look to exempt ill health benefits from the AA regime.

2.9 The Government does not believe that exemptions should be made for individuals being made redundant. Most redundancy packages include an upfront payment, the first £30,000 of which is tax-free. In many cases, the entire redundancy package is less than £50,000.

2.10 The Government expects schemes to adapt to provide individuals with more flexibility of choice on how to take redundancy packages, and for the rare cases where large one-off spikes in pension accrual might occur it believes the carry over of up to three years' unused allowances will offset any excess of AA in a majority of cases.

2.11 The Government intends to set out further details around how exemptions will operate and at the same time how to manage the risks of avoidance that would open up in draft clauses planned for Finance Bill 2011, due to be published for consultation in late 2010.

2.12 The Government is also minded to reduce the lifetime allowance from its current level of £1.8m to £1.5m from April 2012 pending consultation on the detail of its approach.

2.13 Although confirmation of the final details of the new regime's operation has not yet been received, it is expected to the individual members' responsibility to report any excess accrual to HMRC. However, it is expected that scheme administrators will be required to inform members of annual accrual values within prescribed timescales.

3. ACTIONS AND REQUIREMENTS

3.1 A newsletter covering this and an other changea has already been produced and will have been distributed by the time of this meeting. Details will also be posted on to the Fund's website.

3.2 Administration software will need upgrading and employers will have to provide annual contribution returns sooner than at present to enable the administration unit to turnaround the data and produce Annual Benefit Statement within the prescribed HMRC timescales.