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Issue 102: Finance Act - the assent of uncertainty

The taxation of pensions for those with incomes of more than £150,000 remains uncertain, despite Royal Assent being granted to the Finance Act on 21 July. In addition to issues of interpretation, the Act leaves explicit scope for wide-ranging further changes to be made through regulations.

Budget bombshell

April's Budget included a surprise announcement of a new and immediately effective tax charge. The new charge applies to individuals who:

- Have income of more than £150,000 in the current tax year or one of the previous two tax years
- Increase regular pension contributions or benefit accrual, or make irregular contributions
- Have total pension contributions, or earn benefits valued, in excess of £20,000 in the tax year

The charges are targeted at individuals who make changes to their pension arrangements before 6 April 2011, when more fundamental changes to the taxation of pensions for high earners are anticipated. Targeting these individuals with accuracy is difficult. Details of protections aimed at ensuring other individuals are not inadvertently caught by the new charge run to over 50 pages. [These were summarised in our **Analysis**]. It is inevitable that some individuals who are not taking action to deliberately 'forestall' the post 2011 arrangements will be hit by the new charge.

In the Act

Despite a number of anomalies in the original proposals, only one significant amendment has been made in the Act:

- The £20,000 threshold is increased where money purchase contributions have been paid on an irregular basis and these irregular contributions average more than £20,000 over the last three tax years – the increased threshold would be equal to this average, but capped at £30,000.

This provides some additional flexibility, particularly for individuals who make significant contributions on an irregular basis (which is defined as less than every quarter). However, there are several other groups that appear to be treated harshly by the new legislation. During the debate, the Government said that two aspects it would be considering further were:

- Rules relating to new arrangements made on or just before the date of the Budget which may be 'too stringent'
- Additional flexibility for individuals to change personal pension provider without loss of protection.

The Act allows all aspects of the detailed protection rules to be amended through regulation. Although we do not anticipate any of the existing protections being removed, it remains to be seen what additional flexibility will be added.

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Some more clarity
An HMRC Q&A publication has helped to clarify some of the issues left open to interpretation by the legislation. For example, HMRC provides further comment on the treatment of:

- Regular but variable contributions
- Annual renewal of a flexible benefit arrangements
- Benefits enhanced using a discretionary power under the rules
- Employer contributions increased to offset a reduction in member contributions
- Redundancy packages
- Contracting-out rebates

There are several other areas of uncertainty which remain, both in relation to the interpretation of the Act and possible future amendments through regulation.

This is likely to remain a concern for employers for some time, particularly if they are considering:

- Making changes to their pension arrangements
- Carrying out redundancy exercises
- Recruiting senior employees

Although the charge will fall on the individual, the amounts involved could be significant so considering the potential implications is essential.

If you have any questions on this Spotlight please contact your usual Hewitt contact or Peter Williams, (+44 (0) 1372 733763) or visit our website at www.hewitt.com/uk

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