SEPTEMBER **2004**

news

sackers extra pensions reform 2004-05

Tax simplification – the implications for high earners

In the countdown to "A-Day" (6 April 2006), a major concern for employers and trustees of occupational pension schemes is the need to communicate the new system to members. High earners are likely to be a priority because of the difficult choices they face in advance of A-Day.

IR limits

Out with the old...

In with the new...

- From A-Day, there will no longer be any tax limits as such on pension saving.
- Instead, the current eight tax regimes governing occupational and personal pensions will be replaced by two allowances, the Lifetime Allowance ("LA") and the Annual Allowance ("AA").

High earners

Why it matters

- This means that the more generous tax treatment currently enjoyed by those not subject to the earnings cap will disappear.
- Capped high earners may also find that their benefits exceed the new allowances.

The LA

In brief

- Initially £1.5 million, the LA will increase each year until it hits £1.8 million in 2010.
- Whilst pension accrual may exceed the LA, a 25% "recovery charge" will be levied on the excess (or 55% if taken as a lump sum[1]).
- Pensions will be tested against the LA when they vest, with the conversion rate for DB benefits being £1 of pension for every £20 of fund.

The AA

In brief

- Initially £215,000, the AA will also rise each year until it hits £255,000 by 2010.
- The AA will not apply in the final year before a pension comes into payment, provided benefits vest fully.
- Contributions above the AA will be subject to a 40% surcharge.

1 Below the LA, a tax-free lump sum of up to 25% can be taken

High earners

Protecting existing benefits

- Primary Protection will allow individuals whose accumulated pension exceeds the LA at A-Day to escape the recovery charge, provided post A-Day growth remains within certain limits.
- Enhanced Protection will be available whether or not a fund is over the LA at A-Day. *But beware, no post A-Day contributions or accrual will be allowed, although salary-linking (subject to restrictions) can continue for a DB pension.*
- To benefit from these protections, rights will need to be registered by 5 April 2009.

High earners

FURBS and UURBS

- The value of unapproved arrangements (whether funded or not) will not count towards the LA.
- Most of the current tax advantages of FURBS[2] will cease, although there will be some protection for benefits in a FURBS referable to pre A-Day contributions.
- Funds may be transferred from an UURBS[3] to a registered scheme within 3 months of A-Day and will be subject to the LA, although not the AA. Enhanced Protection will not, however, be available.

Action plan

Identify and communicate

- Trustees and employers need to:
  - identify all members whose benefits will exceed (or nearly reach) the LA at A-Day;
  - take into account benefits held in other approved pension arrangements;
  - communicate with those affected as soon as possible;
  - monitor members' benefits going forward to spot in advance those whose benefits are likely to exceed the LA at retirement;
  - consider alternative forms of compensation for key employees.

2 Funded Unapproved Retirement Benefit Schemes
3 Unfunded Unapproved Retirement Benefit Schemes

This edition of Sackers Extra News is the first in a new series focusing specifically on pensions reform. Our Pensions Reform Team will continue to keep you abreast of the key issues throughout this period of pensions simplification. If you would like further information please contact:

Peter Lester	Partner	peter.lester@sacker-partners.co.uk
Eleanor Daplyn	Assistant	eleanor.daplyn@sacker-partners.co.uk

SACKER & PARTNERS

Solicitors specialising in pensions law

29 Ludgate Hill
London EC4M 7NX
Tel 020 7329 6699
Fax 020 7248 0552

enquiries@sacker-partners.co.uk
www.sacker-partners.co.uk