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**Core Unit 3 – Running a Workplace Pension Scheme**

Assignment 3 Notes

(Part 4 – Allowances)

Recommended Time: 2 Hours

1. **Outline the key features of a Pensions Savings Statement.**

**(5 marks)**

Answer should cover:

* must be issued automatically if member exceeds standard AA;
* must be issued within 6 months of tax year end;
* unused AA carried forward and pension input in other schemes not included;
* statement shows pension input amount in the pension input period for current and previous 3 tax years;
* members who don’t exceed AA can request a statement;
* Dc schemes – must issue if individual flexibly accessed DC scheme after 6 April 2015 and pension input amount exceeds Money Purchase AA of £4,000.

Relevant section of the manual is Part 4 Chapter 1.6.

1. **Briefly describe Fixed Protection, Fixed Protection 2014 and Fixed Protection 2016.**

**List the circumstances that may give rise to an individual losing those protections and the information they must provide to HMRC when fixed protection is lost.**

  **(20 marks)**

Answer should cover:

*Fixed Protection – any 4 of the following (4 marks)*:

* Introduced due to reduction in LTA to £1.5m from 6 April 2012
* Available to members if value of their benefits likely to exceed £1.5m by the time benefits drawn;
* Applications for fixed protection had to be received by HMRC by 5 April 2012;
* Benefits up to £1.8m in value protected from Lifetime Allowance charge;
* Future contributions (DC) and future accrual (DB) not permitted.

*Fixed Protection 2014 – any 4 of the following (4 marks)*:

* Introduced as a result of the further reduction in the standard LTA to £1.25m from 6 April 2014;
* Members can protect benefits up to a value of £1.25m;
* Members had to apply for to HMRC before 6 April 2014;
* Future contributions (DC) and future accrual (DB) not permitted;
* Not available to members with primary protection, enhanced protection or fixed protection.

*Fixed Protection 2016 – any 4 of the following (4 marks)*:

* Introduced as a result of the further reduction in the standard LTA to £1m from 6 April 2014;
* Members can protect benefits up to a value of £1m;
* No deadline for applying to HMRC;
* Future contributions (DC) and future accrual (DB) not permitted;
* Not available to members with primary protection, enhanced protection, fixed protection or fixed protection 2014.

*Losing Protection (8 marks)*:

* Protection lost if:
	+ Benefit accrual has occurred;
	+ A transfer that is not permitted has occurred;
	+ There has been a transfer of sums and assets in an arrangement they have under a registered pension scheme that is not a permitted transfer;
	+ They have made a new arrangement under a registered pension scheme other than in permitted circumstances;
* Must provide HMRC with:
	+ full name, address, and National Insurance number;
	+ the exact date that they lost protection;
	+ the reason why they lost protection (for example benefit accrual, auto enrolment);
	+ the type of pension arrangement (defined contribution or defined benefit);
	+ their original certificate (if they still have it.

Relevant section of the manual is Part 4 Chapters 3.2, 3.3, 3.5 and 3.7.

1. **In relation to the Annual Allowance tax charge, briefly describe what is meant by “Scheme Pays”.**

**(5 marks)**

Answer should cover:

* member has the right to require the scheme to pay the charge on their behalf;
* scheme makes appropriate reduction to members’ benefit in return;
* member has right to require scheme to pay if certain conditions met:
	+ member’s AA charge liability for the tax year must exceed £2,000;
	+ pension input amount for scheme must exceed the standard AA;
	+ member must request scheme pays via irrevocable election made in a prescribed form;
	+ deadline for scheme pays request is 31 July after the end of the following tax year.
* scheme can voluntarily pay member’s charge if all conditions not met.

 Relevant section of the manual is Part 4 Chapter 1.5.

1. **Describe the key features of the Lifetime Allowance (LTA) and list the Benefit Crystallisation Events (BCEs) which would trigger a test of a member’s benefits against the LTA.**

**(20 marks)**

Answer should cover:

*LTA (10 marks)*:

* Broadly, LTA is an allowance of the total pension rights an individual may accrue in their life in registered pension schemes while still benefiting from tax relief;
* when BCE is triggered, part of their LTA is used up;
* Lifetime Allowance Charge applies when there is no longer any remaining LTA and further benefits put into payment;
* LTA charge set at a level intended to remove the tax advantages previously received in relation to those benefits because of their membership of a registered pension scheme;
* overall effect - benefits with total value up to the LTA will enjoy the tax advantages of a registered pension scheme, but the taxation of any benefits above this level is intended to be broadly neutral;
* The level of the LTA Charge depends on whether the benefits subject to the charge are taken in pension or lump sum form;
* LTA introduced from 6 April 2006 at the level of £1.5 million and increased gradually to £1.8m (2010/11);
* Finance Act 2011 – individuals could apply for protection against reduction from £1.8m to £1.5m LTA from 2012/13;
* Finance Act 2013 – individuals could apply for protection against reduction from £1.5m to £1.25m LTA from 2014/15;
* Finance Act 2016 – individuals could apply for protection against reduction from £1.25m to £1m LTA from 2016/17;
* Finance Act 2016 – LTA to increase in line with CPI from 2018/19;
* Finance Act 2021 – link to CPI increase removed.

*BCEs – any 10 of the BCEs from the following table (10 marks)*:



 Relevant section of the manual is Part 4 Chapters 2.1 and 2.2.

# Explain the Tapered Annual Allowance and provide an example of a tapered AA calculation.

**(10 marks)**

Answer should cover:

* Key features of the AA (6 marks):
	+ Effective from 6 April 2006 (A-day) for high earners;
	+ Range of tapered AA between £4,000 and £40,000;
	+ Threshold income – broadly total taxable income;
	+ Adjusted income – broadly taxable income plus pensions savings;
	+ 2 income tests apply:
		- whether threshold income exceeds £200,000;
		- whether adjusted income exceeds £240,000;
	+ where both tests passed, AA reduces by £1 for every £2 of adjusted income above £240,000;
* A worked example showing the tapered AA for a high earner (4 marks).

Relevant section of the manual is Part 4 Chapter 3.9.2.

1. **The initial level of the Annual Allowance (AA) was £215,000, effective from 6 April 2006 (A-day).**

**Explain how the amount of the AA has changed since A-day.**

  **(10 marks)**

Answer should cover:

* AA increased by £10,000 every tax year until 2010/11 when it was £255,000;
* Finance Act 2011;
	+ reduced AA to £50,000 effective 2011/12 tax year, due to:
		- state of the public finances and the consequent need to raise revenue;
		- fear that the 50% additional rate of Income Tax introduced in 2010/11 would prompt

high earners to put excessive amounts into pension schemes to avoid (or defer) tax;

* AA charge of 40% abolished;
* pension input amount (PIA) added to earnings and taxed at the individual’s marginal rate:
	+ PIA over higher rate tax limit taxed at 45%;
	+ PIA over basic rate limit but below higher rate tax limit taxed at 40%;
	+ PIA below lower rate tax limit taxed at 20%;
* removal of exemption for members with Enhanced Protection;
* removal of exemption for those who draw all their benefits from the scheme;
* introduction of” carry forward” – unused AA can be carried forward from the previous three tax years to cover excess pension savings over the AA in the current tax year;
* special rules introduced relating to the calculation of PIPs for the period 14 October 2010 to 5 April 2011.

Relevant section of the manual is Part 4 Chapter 1.1.

1. **Briefly outline how an individual’s pension rights are valued in order to determine whether they exceed the Lifetime Allowance, and provide a worked example.**

**(10 marks)**

Answer should cover:

* HMRC laid down a set of criteria for valuing pension rights when they are crystallised;
* DC scheme – value generally taken as the fund value at the time of crystallisation;
* DB scheme - value is the amount of any cash sum taken plus 20 x the starting pension;
* The value for a money purchase pot used to provide a scheme pension is also 20 x the starting pension;
* a pension that was put into payment prior to 6 April 2006 is also tested - at the time of the first post 6 April 2006 BCE;
* value of pre 6 April 2006 pension is the pension in payment at the time of the first BCE x 25;
* total value of the pension rights is then deducted from the member’s Lifetime Allowance;
* worked example showing value of pension rights and tes t against LTA.

 Relevant section of the manual is Part 4 Chapter 2.3.

1. **Describe the purpose and key features of the Pension Input Amount, in relation to the Annual Allowance.**

**(15 marks)**

Answer should cover:

 *DC Scheme (5 marks)*:

* pension input amount is the total ‘relievable contribution’ paid by or on behalf of the member in the pension input period;
* includes AVCs paid by the member but excludes transfers into the scheme from other arrangements;
* Taxation of Pensions Act 2014 introduced a Money Purchase Annual Allowance from 2015/16 tax year;
* MPAA limit £10,000, reduced to £4,000 from 6 April 2017;
* MPAA only applies to pension input amounts in DC arrangements when individual has flexibly accessed a DC arrangement
* MPAA does not apply if individual has not flexibly accessed a DC arrangement.

*DB Scheme (7 marks)*:

* pension input amount is difference between value of a person’s benefits at the end of the pension input period is compared with the value of their benefits at the end of the previous pension input period;
* inputs relating to the 2010/11 and earlier tax years:
	+ a factor of ten is used to value the benefits;.
	+ adjustments made to the figures to take account of transfers in or out of the scheme and pension debits or credits;
	+ further adjustment for deferred DB member - ensures that the normal annual revaluation not included in pension input amount;
* inputs relating to the 2011/12 and later tax years:
	+ valuation factor of 10 replaced by 16;
	+ inflation protection extended to active members;
	+ deferred members whose benefits’ revaluation does not exceed the increase in the CPI deemed as having no pension input amount;
* individual subject to MPAA still entitled to the alternative Annual Allowance for ‘other inputs’;

*Short worked example of pension input amount calculation and comparison to AA (3 marks)*

Relevant section of the manual is Part 4 Chapters 1.2 and 1.3.

1. **In relation to the Annual Allowance tax charge, briefly describe what is meant by “Scheme Pays”.**

**(5 marks)**

Answer should cover:

* member has the right to require the scheme to pay the charge on their behalf;
* scheme makes appropriate reduction to members’ benefit in return;
* member has right to require scheme to pay if certain conditions met:
	+ member’s AA charge liability for the tax year must exceed £2,000;
	+ pension input amount for scheme must exceed the standard AA;
	+ member must request scheme pays via irrevocable election made in a prescribed form;
	+ deadline for scheme pays request is 31 July after the end of the following tax year.
* scheme can voluntarily pay member’s charge if all conditions not met.

 Relevant section of the manual is Part 4 Chapter 1.5.