

April Budget and Finance Act 2009

The changes in detail

We hope this brief note, about the impact of Alastair Darling's April Budget, will be of assistance to advisers and their clients alike.

We have seriously mixed feelings about the changes that are to be implemented in April 2011 and, of course, the immediate effect of the "anti-forestalling" measures operative from Budget Day 22nd April.

It has to be said that the £150k limit will only affect a very small percentage of pension savers (probably no more than 1%-2% of the working population according to Government statistics). It is likely that that percentage will be somewhat higher for your clients and our SIPP clients but will still be comparatively small.

However, perhaps the real damage, other than to those who are directly affected, is to the perception of pensions generally.

The loss of higher rate relief for high earners (and the previously enacted change of retirement age from 50 to 55, effective April 2010) can do no favours to the message that saving for retirement is a sensible / attractive course of action. It clearly is but this constant "tinkering" with the ground rules is surely counter productive.

We believe the Budget changes are largely politically motivated and, in reality, will have little impact on the yawning gap in Government finances.

So, after that "rant" what are the changes?:-

From April 2011

Those with relevant income below £150,000 are simply not affected. Tax relief at the highest marginal rate will continue to be available for personal contributions up to 100% of earnings. Total contributions up to the annual allowance (typically a combination of employer and employee contributions) will remain as tax efficient as ever.

It is important to note that the definition of income for this purpose is not simply "net relevant earnings" as we know it but effectively includes all forms of income.

There is a six stage process in calculating the precise figure as follows:-

1. Earnings from employment (salary, bonus, P11D benefits), earnings from self employment/partnerships, pensions income, interest on most savings, dividend income from shares, rental income, income received from a trust.

Amounts detailed in Sections 30 and 32 of ITA 2007 need not be included.

Please contact us if you would like more information on this particular aspect.

PLUS

2. Any pension contributions made as part of a net pay arrangement

LESS

3. Certain losses and other reliefs. Here reference is made to some 10 different sections of The Income Tax Act 2007 where deductions may be allowed!!

LESS

4. The amount of pension contributions made during the tax year but subject to a maximum deduction of £20,000.

PLUS

5. Any contributions made by means of salary sacrifice.

LESS

6. Any amounts that represent donations for "gift aid"

The reference made to so many sections of ITA 2007 is a fairly clear demonstration that this calculation is not, necessarily, a simple one! No doubt if the client's situation is in any way "borderline" advisers will wish to enlist the help of the accountant

For those with income, calculated as above, in excess of £150,000 higher rate relief on contributions is to be curtailed such that it is reduced to ZERO on incomes over £180,000. (Client's pension still receives 20% basic rate relief via the normal reclaim at source) By that time, of course, the top rate of tax will be 50% and, whilst it is not specified, one assumes the reduction will be on a simple one for one basis.

Is it obtuse that a client earning £140k will be able to pay £140k contribution and enjoy a total 40% relief and yet someone with income of £180k will only receive 20% relief on the same contribution of £140k?

There are just a few exemptions which, for these high income clients and depending on circumstances, may be helpful:-

- Contributions up to £20,000 (known as the special annual allowance) are not affected
- "Regular" contributions in excess of £20,000 may be continued without any problem. However the definition of regular is somewhat obscure and is "quarterly or more frequently". Whilst we're all used to seeing gas and electricity bills being paid on a quarterly basis we're not aware of a great many SIPP clients who pay contributions at this frequency! In reality, for the vast majority of pension savers "regular" really means monthly and so regular contributions in excess of £1666.66 per month may be continued without difficulty.
- In addition any pre-determined increases in those regular contributions (as a result of salary increases etc) are also exempt.
- In an 11th hour amendment to the legislation some relaxation is available to those who pay on a less than "regular" basis. This will be of some help to the self employed who fairly typically pay "ad hoc" singles depending on the profitability of their business. Here one can take an average of the last three years (06/07, 07/08, 08/09) contributions that have been paid when determining the special annual allowance. It is important to note however that this easement is capped at £30,000 contribution. Furthermore some care needs to be taken as any regular monthly payments that are currently being made "interact" in the calculation.

There is one quirk in the legislation which really must be addressed sooner rather than later. As it stands any client who is benefitting from the protected pension input nature of "regular contributions" will lose that exemption if he, no doubt for perfectly valid reasons, chooses to stop paying to the current provider and start contributions (at precisely the same level) to a new pension. Government is aware of this inequity and have suggested the matter will be considered and hopefully be amended through regulation. Surely if any heed whatsoever is taken of the concept of "treating customers fairly" then this will be addressed sooner rather than later!

Anti forestalling provisions effective from Budget Day 22nd April 2009

Quite clearly, and perhaps even understandably, Government are concerned that having set out the legislation from April 2011 there would be an abundance of very large contributions between now and then on a "buy now while stocks last basis"

To guard against this anti-forestalling provisions are in place and had immediate effect from Budget Day 22nd April 2009. (There is some controversy about contributions paid on or just before Budget Day and this has yet to be clarified)

The result is that any contributions exceeding the limits and paid by high income clients (both as described as above) will incur a personal tax charge of 20%.

The client will still claim higher rate tax relief through their normal self assessment return but this will simply be negated by the 20% charge. Stating the obvious they now only benefit from 20% basic rate tax relief on their personal contributions.

Conclusions and some positive news

So does this represent the death of pensions and SIPPS in particular? Very emphatically of course not! The vast majority of clients, who have relevant income of less than £150,000, are completely unaffected and higher rate tax payers will continue to enjoy up to 40% tax relief as before.

The challenge now exists for the unfortunate (definite sic here!) few who earn more than £150,000.

From the advisers perspective these clients need your advice more than ever!

May we suggest that the concept of SIPP property purchase is even more compelling than ever it was?

Consider that from April 2010 tax rates will be at 50%. **The ability to pay rent from your business into your pension and enjoy 50% tax relief thereon will become incredibly attractive.**

We have considerable experience of SIPP property purchase (both new purchases and "in specie" contribution of existing property). There are certain techniques and strategies that your clients can use to minimise the impact of the Budget changes and position themselves to enjoy maximum tax reliefs going forward.

If you would like to meet with one of our pensions consultants to explore these opportunities please do not hesitate to contact us