

ANNUAL ALLOWANCE
WHO'S AFRAID OF THE BIG BAD CHARGE?



AA – WHO'S AFRAID OF THE BIG BAD CHARGE?

LEARNING OBJECTIVES

At the end of this session you will have an understanding of:

- how the annual, money purchase, and tapered allowances work
- Illustrate the different considerations which are applicable in a an AA charge scenario

ANNUAL ALLOWANCE

WHO'S AFRAID OF THE BIG BAD TAX CHARGE?

AA/MPAA/TAPER – A REFRESH

AA – WHO'S AFRAID OF THE BIG BAD TAX CHARGE? THE ANNUAL ALLOWANCE

AA

- £40,000*
- Charge on pension input amount (PIA) exceeding AA in the PIP
- PIPs now aligned with tax years
- PIA:
 - DC = contributions paid
 - DB = growth in benefits over PIP

*For those with taxable incomes not exceeding £150,000.00
An additional restriction applies to individuals who have taken benefits flexibly

AA – WHO'S AFRAID OF THE BIG BAD TAX CHARGE? **CARRY FORWARD**

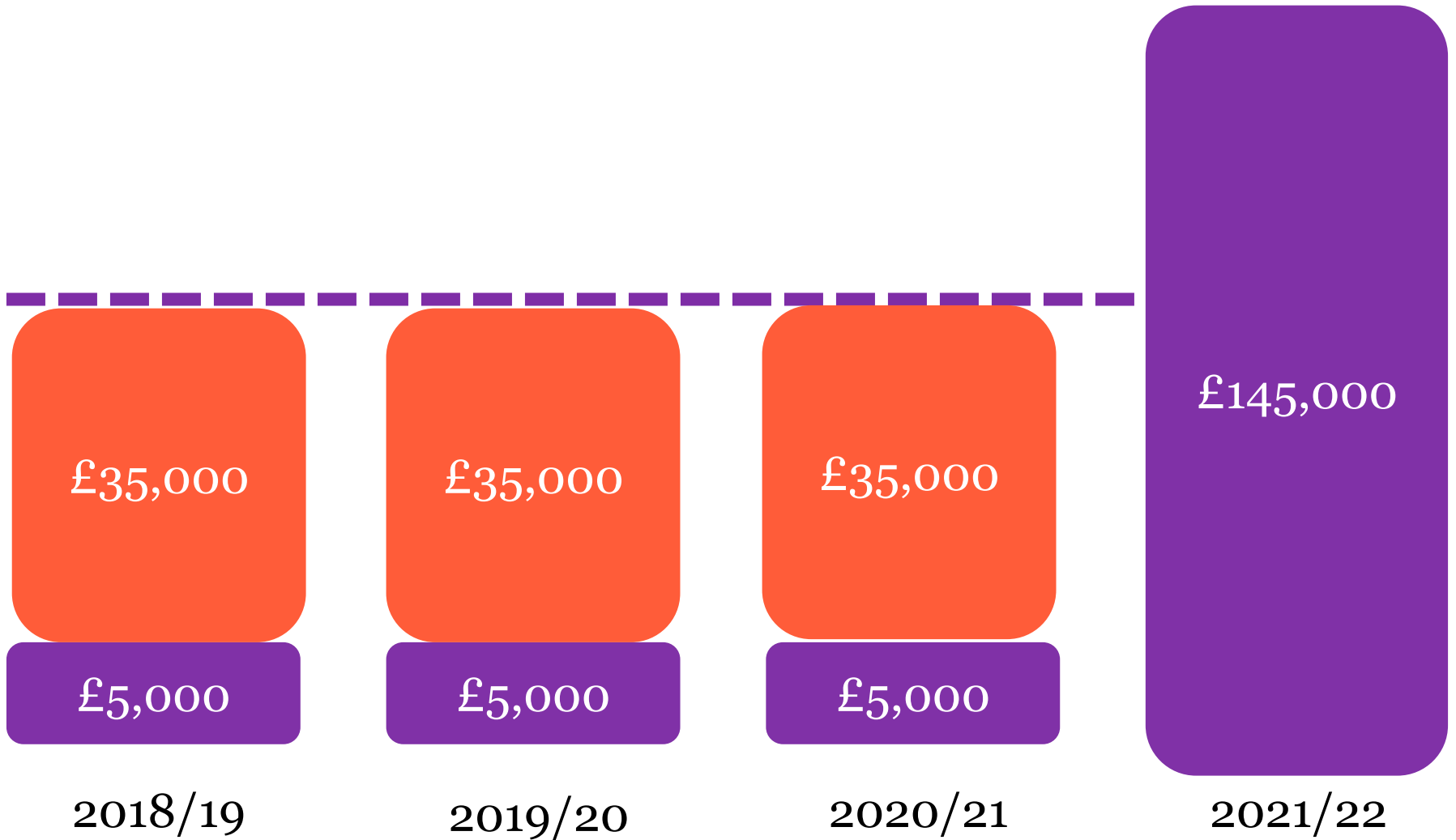
Up to 3 years of unused annual allowance

Member of a pension scheme in the relevant year

Current year's AA first....then earliest year

No offset against MPAA

THE BUSINESS OWNER THE ANNUAL ALLOWANCE – USE IT OR LOSE IT



AA – WHO'S AFRAID OF THE BIG BAD TAX CHARGE? **THE MPAA**

MPAA

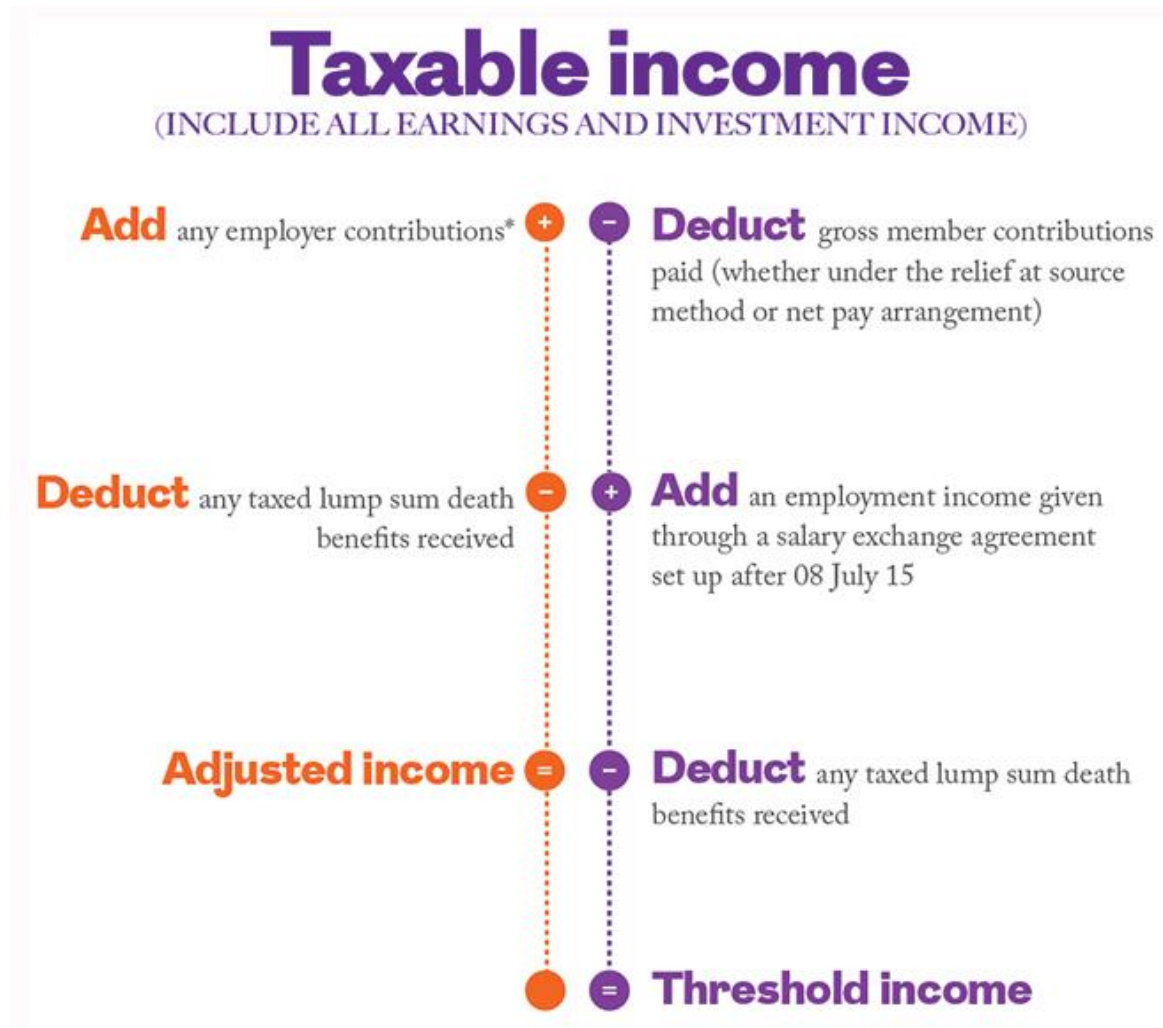
- Applies when DC benefits are “flexibly accessed”
- Is currently £4,000.00
- Measured over the PIP
- No carry forward

AA – WHO'S AFRAID OF THE BIG BAD CHARGE? THE TAPERED ANNUAL ALLOWANCE

Tapered AA

- Effective 6 April 2016
- Adjusted income > £150,000
AND
- Threshold income > £110,000
- Reduces AA £1 for £2
- Minimum £10k allowance

AA – WHO'S AFRAID OF THE BIG BAD TAX CHARGE? THE TAPERED ANNUAL ALLOWANCE



*For DB schemes this will be the pension input amount less employee contributions

THE BUSINESS OWNER

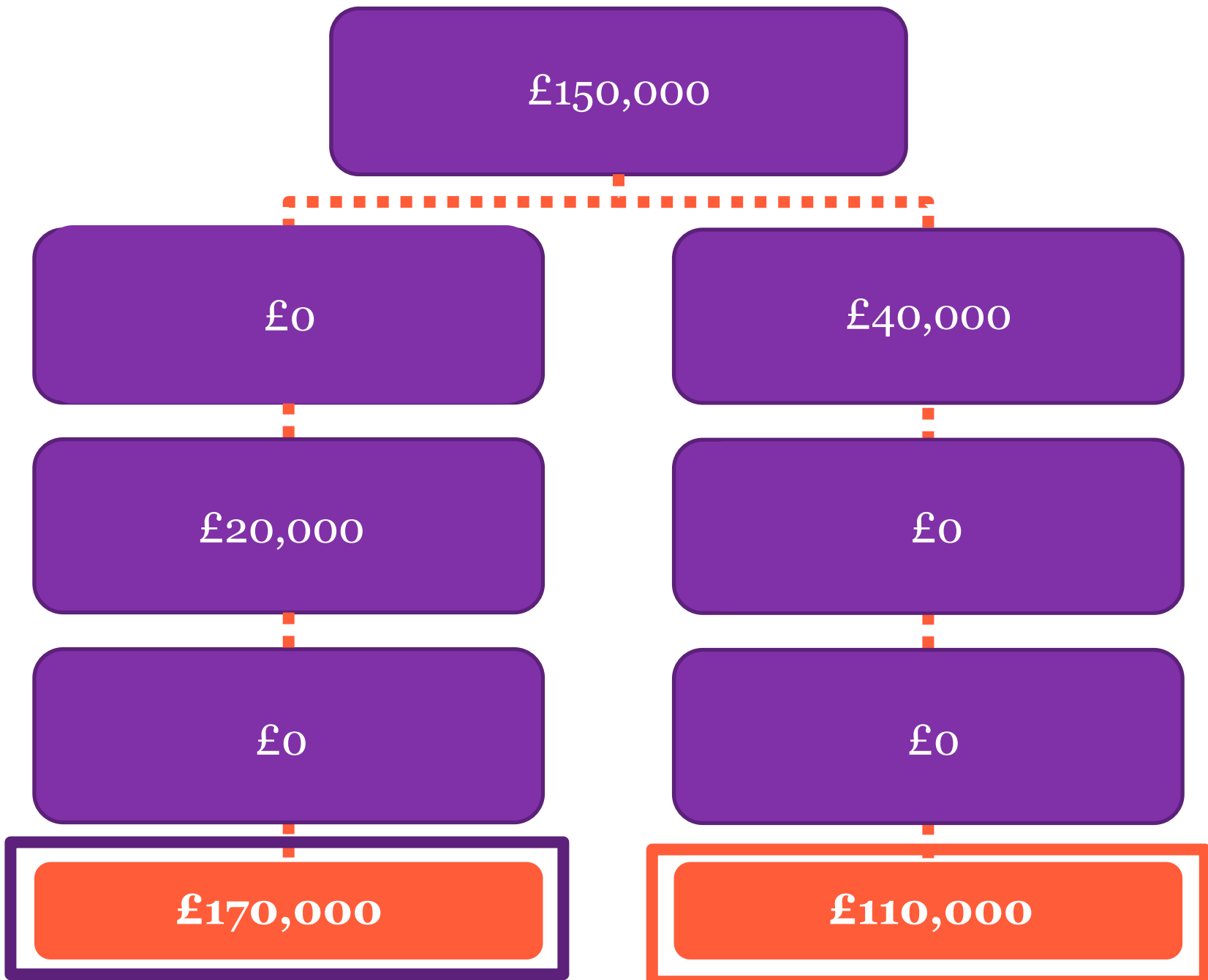
THE TAPERED ANNUAL ALLOWANCE

Example :

Harold is a director who has taxable income of £150,000 gross and:

- he's paid an employer contribution of £20,000 plus an individual contribution of £20,000 into his SIPP
- and has carried forward £20,000 from previous tax years as a personal contribution

What is Harold's annual allowance?



* The individual's net income for the tax year as calculated under steps 1 and 2 of section 23 of the Income Tax Act 2007

ANNUAL ALLOWANCE

WHO'S AFRAID OF THE BIG BAD TAX CHARGE?

THE CALCULATION PROCESS

AA – WHO'S AFRAID OF THE BIG BAD TAX CHARGE? MEMBER STAYS IN

1

- Calculate value of benefits now/at retirement
- Contributions/investment returns

2

- Calculate cost of remaining in scheme
- Rate of tax relief

3

- Calculate benefits net of any tax charge
- Scheme pays arrangements/factors

AA – WHO'S AFRAID OF THE BIG BAD TAX CHARGE? MEMBER OPTS OUT

4

- Calculate value of deferred benefit (at retirement)
- Investment return. Revaluation results

5

- Identify value of alternative arrangements (if any)
- Investment return

6

- Compare deferred benefit value to value of alternative arrangements

Compare outcome of 3 and 6

ANNUAL ALLOWANCE

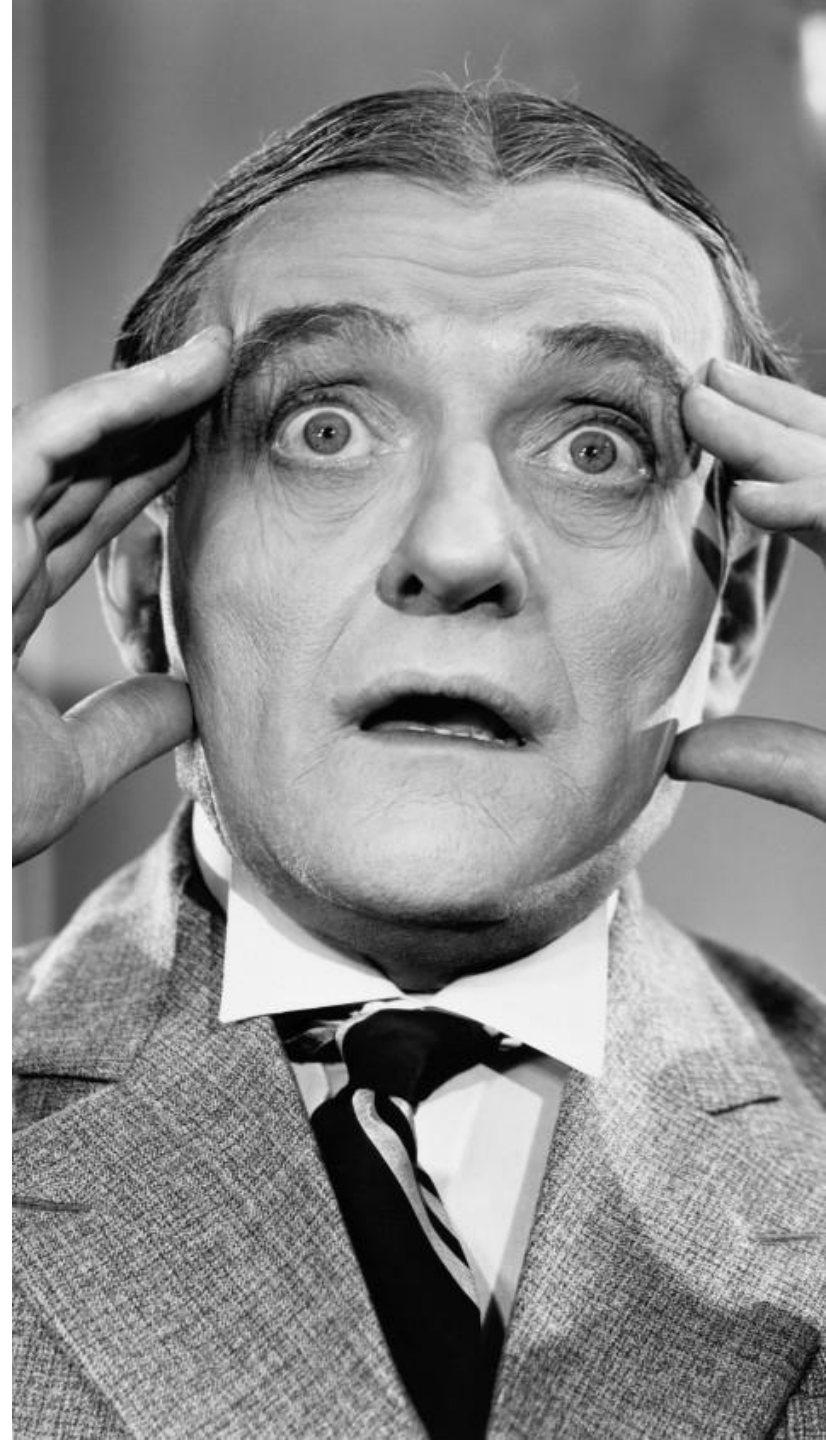
WHO'S AFRAID OF THE BIG BAD TAX CHARGE?

CASE STUDY

WHO'S AFRAID OF THE BIG BAD TAX CHARGE?

DC CASE STUDY

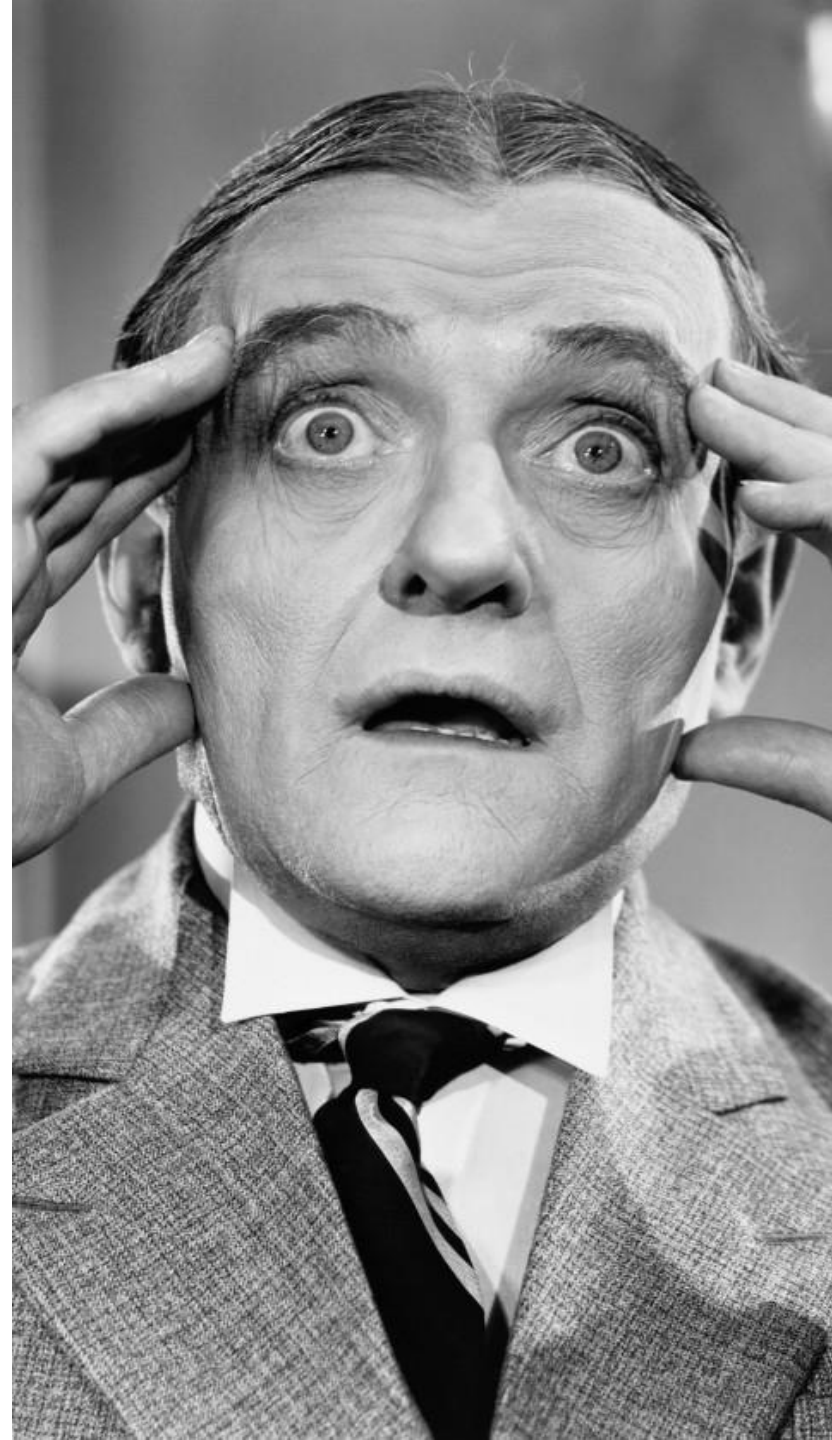
- Meet Karl
 - Age 50
 - Salary = £215,000
 - No carry forward
 - Employer contributions = 8%
 - Matching contributions 1 for 1 to 6%
 - Expects to retire in 10 years



WHO'S AFRAID OF THE BIG BAD TAX CHARGE?

DC CASE STUDY

- Karl's Options:
 - Employer contributions only
 - Employer + employee of 20%
 - Leave scheme. Alternate strategy?



AA – WHO'S AFRAID OF THE BIG BAD TAX CHARGE? DC CASE STUDY – KARL STAYS IN EMPLOYER CONTRIBUTION ONLY

1

- Value now $8\% * £215,000 = £17,200$
- **Employer contribution rate is 8%**

2

- Cost to Karl = £0.00

3

- Benefit net of tax charge at retirement
- $£17,200 - (£7,200 * 45\%) * 1.04^{10} = £20,664$

Net of charges, growth over the 10 years to Karl's retirement is assumed to be 4%

AA – WHO'S AFRAID OF THE BIG BAD TAX CHARGE? DC CASE STUDY – KARL STAYS IN EMPLOYER + EMPLOYEE CONTRIBUTIONS

1

- Value now $20\% * £215,000 = £43,000$
- 14% employer (standard + matching)
- 6% employee

2

- Cost to Karl
- $£215,000 * 6\% * 55\% = £7095$
- Karl receives tax relief at 45%

3

- Benefit net of tax charge at retirement
- $£43,000 - (£33,000 * 45\%) * 1.04^{10} = £41,669$
- Karl pays a tax charge on £33,000 at 45%

Net of charges, growth over the 10 years to Karl's retirement is assumed to be 4%

AA – WHO'S AFRAID OF THE BIG BAD TAX CHARGE? DC CASE STUDY – KARL OPTS OUT

4

- Calculate value of deferred benefit (at retirement)
- **FUM only**

5

- Identify value of alternate arrangements
- £14,802 (£10,000 PP invested over 10 years)
- **Net growth assumed to be 4%**

6

- Add deferred benefit value to value of alternate arrangements
- **FUM + £14,802**

KARL – OUTCOME COMPARISON

	Employer contributions	Employer + employee contributions	Leave scheme/ alternate strategy
Value in 10 years	FUM + £20,664*	FUM + £41,669*	FUM + £14,802
Net cost to Karl	£0.00	£7,095	£5,500
Net benefit	£20,664*	£34,574*	£9,302

* Value AFTER AA charge

WHO'S AFRAID OF THE BIG BAD TAX CHARGE?

WIDER CONSIDERATIONS

- Dependants' benefits
- Ill-health benefits
- Distribution of death benefits
- Public sector – “protections”
- Wider tax implications



WHO'S AFRAID OF THE BIG BAD TAX
CHARGE?
WIDER CONSIDERATIONS - KARL

Karl leaves his scheme:

- Dependants benefits:
 - Continuing dependants' entitlement to FUM
 - No entitlement to DIS lump sum (insured risk)
- No impact on ill health retirement
- Wider tax implications:
 - No impact on taper
 - No impact on Personal Allowance
 - Income tax on 6% more of salary
 - PP – IHT status of death benefits



AA – WHO’S AFRAID OF THE BIG BAD TAX CHARGE? **KARL – RECOMMENDATION**

	Employer Contributions	Employer + Employee Contributions	Leave scheme/ Alternate Strategy
Value in 10 years	FUM + £20,664*	FUM + £41,669*	FUM + £14,802
Net cost to Karl	£0.00	£7,095	£5,500

* Value AFTER AA charge

RECOMMENDATION:

Stay in occupational scheme. Employer + employee contributions
Make scheme pays election
Regular reviews

AA – WHO'S AFRAID OF THE BIG BAD CHARGE?

LEARNING OUTCOMES

At the end of this session you will have an understanding of:

- Consider how the annual, money purchase, and tapered allowances work and the charges applicable.
- Illustrate the different considerations which are applicable in a an AA charge scenario.



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**LIFETIME ALLOWANCE
TAKE IT TO THE LIMIT....
& BEYOND?**

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LIFETIME ALLOWANCE LEARNING OBJECTIVES

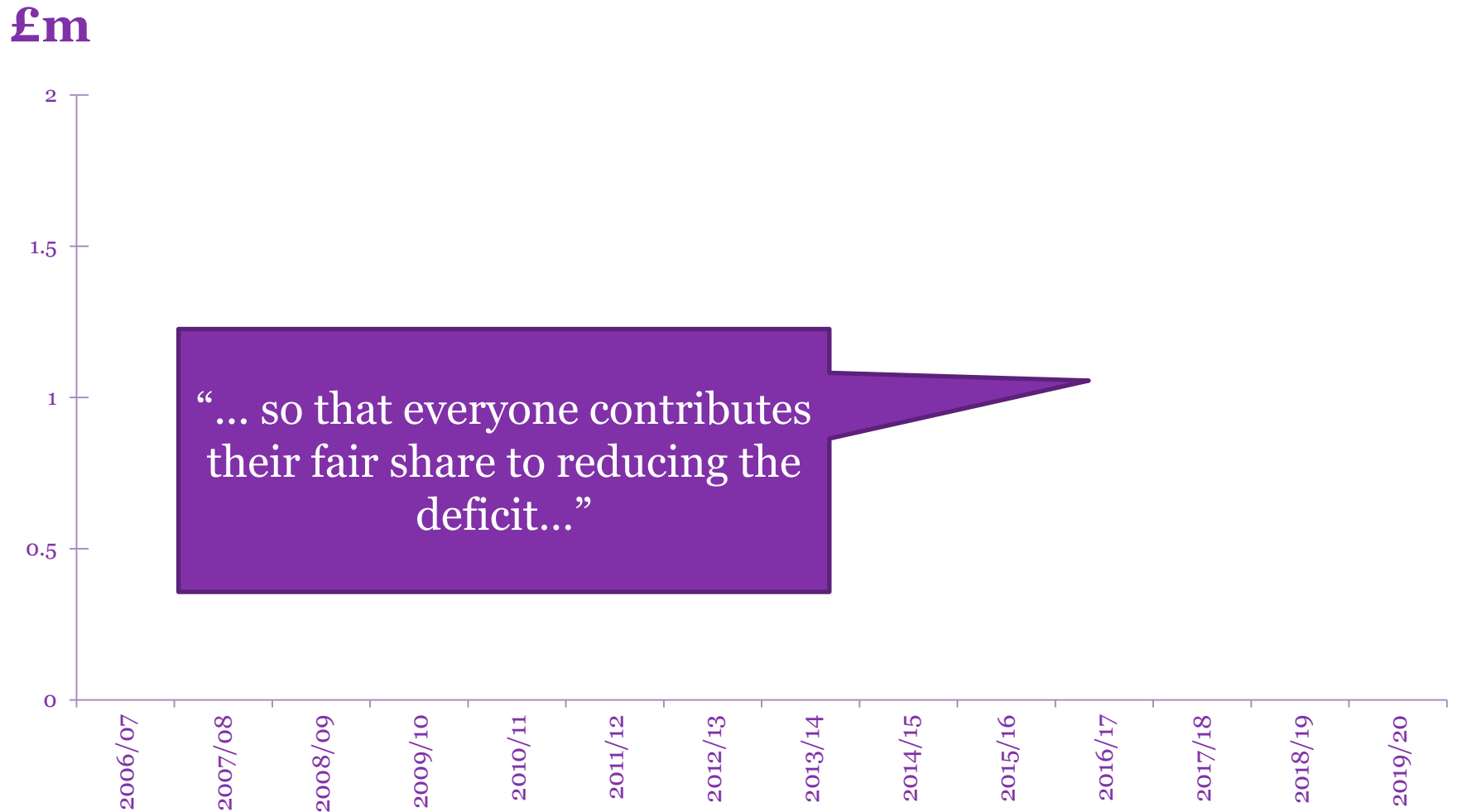
At the end of this session you will have an understanding of:

- How the lifetime allowance works and the various protections available



**LIFETIME ALLOWANCE
RESTRICTING TAX RELIEF**

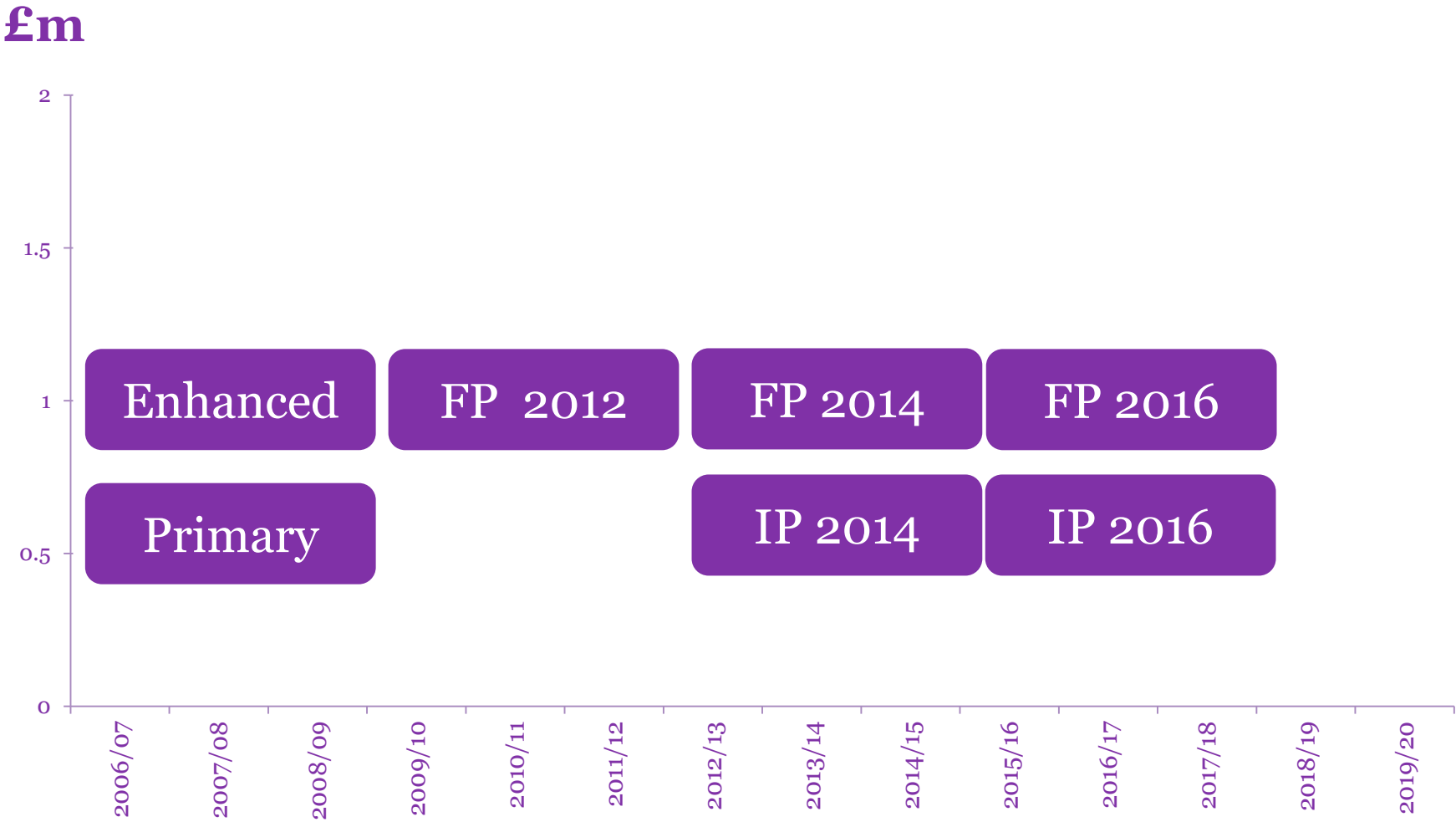
LIFETIME ALLOWANCE RESTRICTING TAX RELIEF





LIFETIME ALLOWANCE
PROTECTION

LIFETIME ALLOWANCE PROTECTION



Source: Royal London & Budget 2015

LIFETIME ALLOWANCE PROTECTION

Fixed Protection 2016

- Keeps LTA at £1.25 million after 06/04/2016
- Available to anyone who doesn't have Primary, Enhanced or Fixed 2012/2014
- Lost if contributions made or further accrual above the 'relevant percentage' occurs
- Can be held in conjunction with Individual Protection 2016

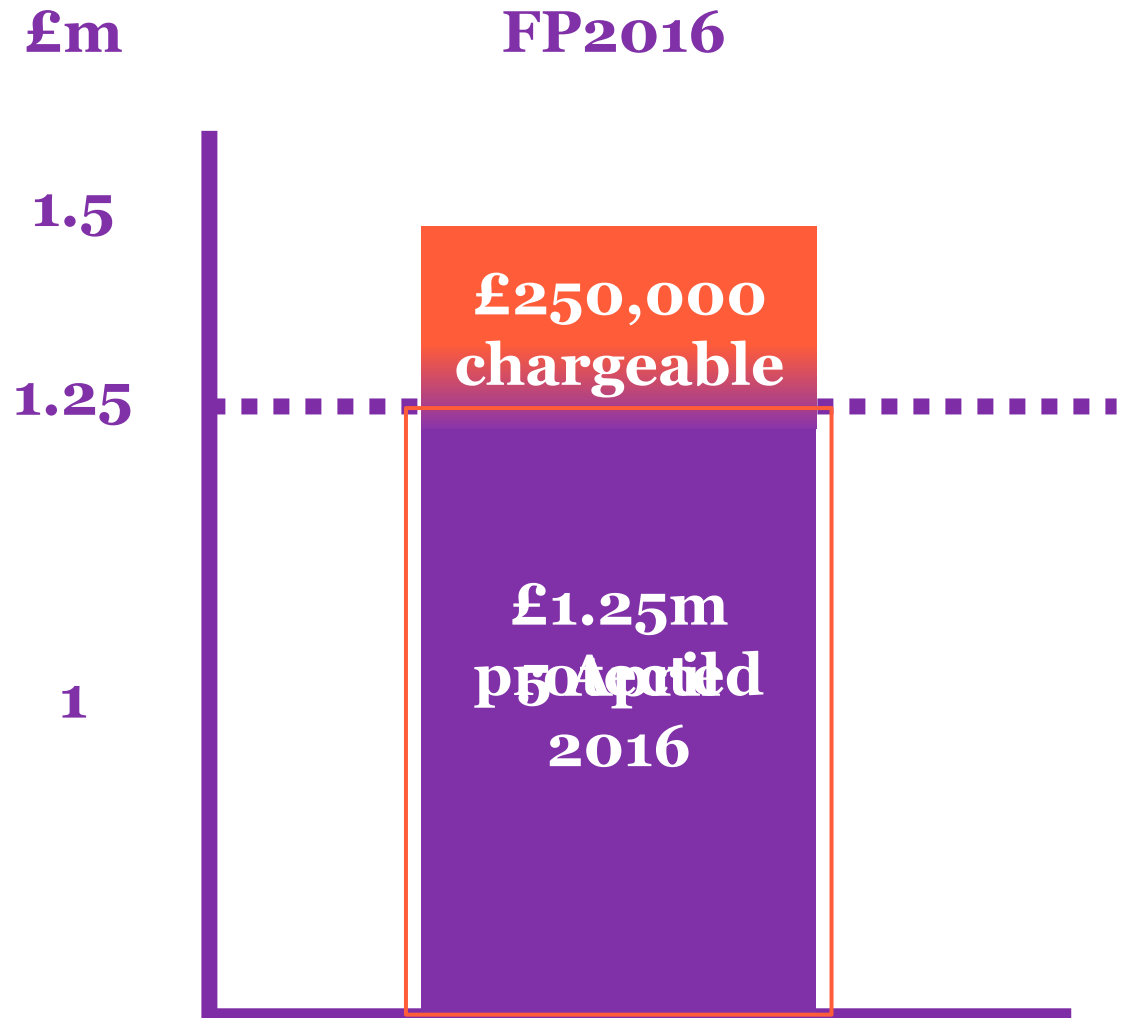
Individual Protection 2016

- Must have pension savings of more than £1m at 05/04/2016
- Protects members LTA at pot level subject to maximum of £1.25m
- Can continue with pension contributions
- Unavailable in conjunction with Primary Protection or IP 2014

LIFETIME ALLOWANCE FIXED PROTECTION

Example 1

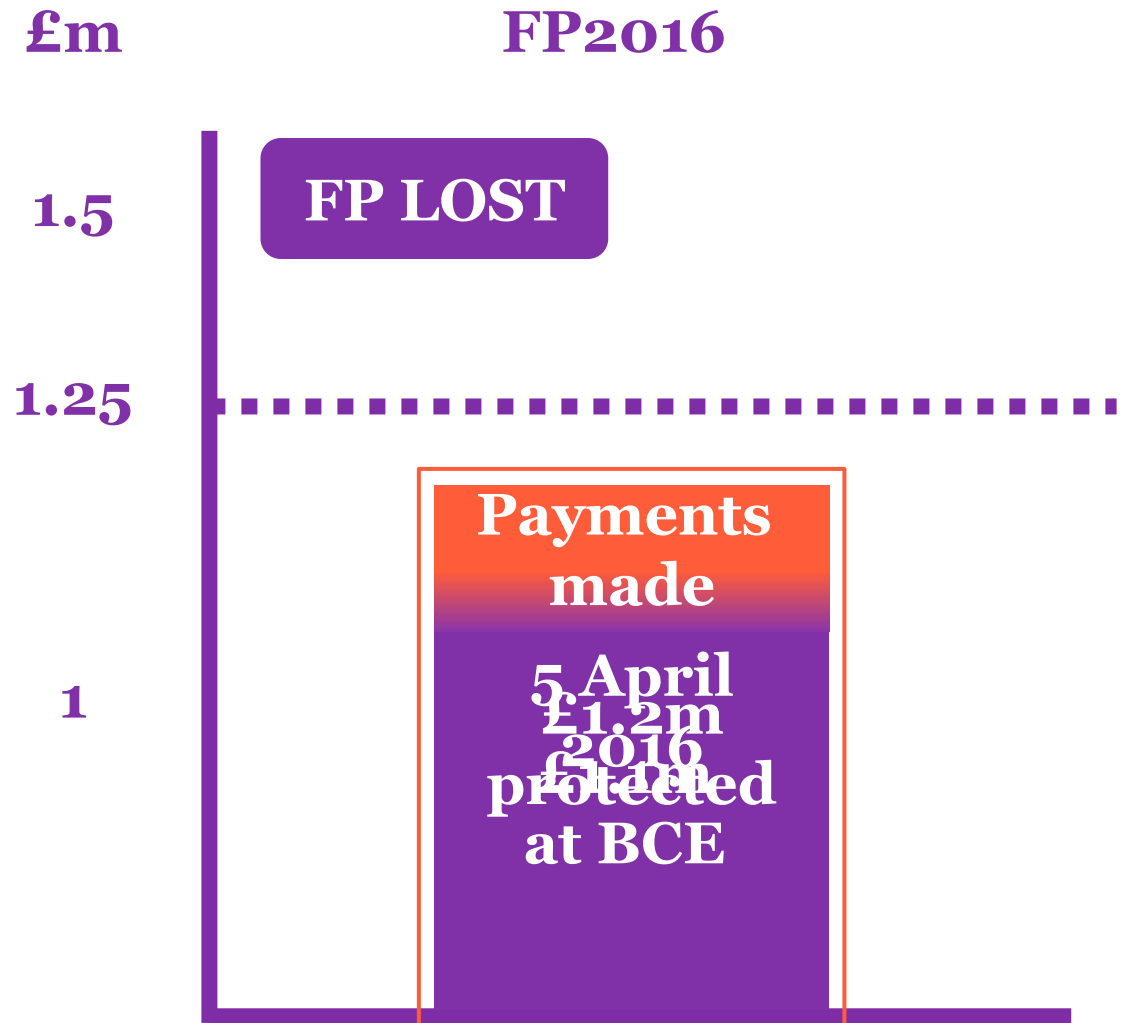
- Fund value of £1.2m at 5 April 2016
- Applied for FP2016
- No further contributions made
- £300k investment growth to BCE



LIFETIME ALLOWANCE FIXED & INDIVIDUAL PROTECTION

Example 2

- Fund value of £1.2m at 5 April 2016
- Applied for FP & IP 2016
- **Poor** investment performance
- Fund value **drops** to £1.1m



LIFETIME ALLOWANCE **PROTECTION**

FP2016 suitable where:

- Fund value likely to exceed LTA in future
- Even without further contributions

IP2016 suitable where:

- Fund value is more than £1m on 5 April 2016
- Might want to make more payments
- Employer only payments

LIFETIME ALLOWANCE OPTIONS

Options when Lifetime Allowance exceeded:

1

Take all the excess as cash @ 55% LAC

2

Take all the excess as income @ 25% LAC

3

Don't touch the excess yet – no immediate LAC

4

Do nothing until LTA test forced



THANK
YOU