



Pensions anti-forestalling - the special annual allowance charge

From 6 April 2011 onwards, the Government has announced that tax relief on pension contributions for individuals with an annual income of £150,000 or more may be restricted to the basic rate. In anticipation of this change, there is a special annual allowance (“SAA”) and associated tax charge from 2009-10 that may apply to contributions made prior to 6 April 2011.

The charge applies only in respect of individuals

- who have relevant income of £130,000 or more in certain tax years and
- have made pension saving on or after the relevant cut-off date that is not *protected* from the charge and
- whose total pension saving in a tax year is greater than their SAA.

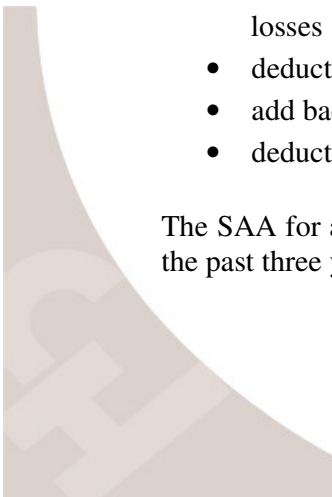
There are effectively two slightly different sets of rules. The relevant cut-off date is 22 April 2009 for individuals with relevant incomes of £150,000 or more and 9 December 2009 for individuals with relevant incomes of £130,000 and over but less than £150,000.

Relevant income for a tax year is the amount of income that relates to the individual in that tax year, and in either of the two previous tax years. The starting point for calculation is the total of the individual’s general taxable income, which is then subject to various adjustments, including:

- add pension contributions under a net pay arrangement
- deduct various reliefs including qualifying interest payments and trade and property losses
- deduct relievable personal pension contributions (maximum £20,000 gross)
- add back salary sacrifice agreed on or after the relevant cut-off date
- deduct Gift Aid donations

The SAA for an individual is £20,000 (or the lower of £30,000 and average contributions over the past three years if contributions are less regular than quarterly).

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However, the amount of an individual's SAA is reduced to take account of:

- certain pension saving that has continued to be made on a regular basis since before the relevant cut-off date (*protected amounts*) and
- for the 2009-10 tax year, contributions made between 6 April 2009 and the relevant cut-off date.

Broadly, where total contributions, including employer contributions, again reduced by the two points above, exceed the SAA, any excess is subject to the special annual allowance charge, which for 2009-10 is at a rate of 20%. For 2010-11, the rate will be such that the tax relief is reduced to, rather than by, 20%. The tax charge is collected through the individual's self-assessment return.

In certain cases, contributions may be subject to both the annual allowance charge and the SAA charge. Where this happens there is a provision to prevent a double tax charge.

Impact on the family company

The new rules present a significant problem for the family company where the practice has been to pay a modest salary plus a dividend to the owners plus an annual pension contribution by the company. This has been seen as a tax efficient way of extracting profits because the pension contribution has been allowable for corporation tax purposes and not charged as a benefit in kind on the director. Great care will be needed in considering profit extraction over the next two years.

Example

Alastair is a director of Midlothian Ltd. Over the past three years the position has been as follows:

Year end 31 March	2007	2008	2009
Salary	£10,000	£10,000	£10,000
Dividend	£100,000	£125,000	£70,000
Pension Contribution	£25,000	£30,000	£25,000

In the 2009 year the business suffered from the effects of the recession but business has picked up again. Alastair is now 50 years old and would like to increase his pension provision and so he has in mind making the same provisions for salary and dividend but increasing the pension contribution by the company to £50,000.

He will be caught by the provisions because his relevant income exceeded £130,000 in 2007-08. The SAA in this case will be based on the relevant mean of the contributions and will be

£26,666. If the company makes a contribution of £50,000, Alastair will have an SAA charge of:

$$(\pounds 50,000 - \pounds 26,666) \times 20\% = \pounds 4,666.80$$

