

This leaflet is solely for the use of financial and other professional advisors

THE ANNUAL ALLOWANCE

Each tax year, HM Revenue & Customs (HMRC) set an 'Annual Allowance' on the level of tax relivable pension savings each person can benefit from in that year. This is an aggregate measure over all the registered pension schemes of which they are a member in that tax year.

The Annual Allowance is £50,000 for tax years 2011/12 and 2012/13 and will remain fixed at that level until at least 2015/16. It may be reviewed in 2015/16

What counts against the Annual Allowance?

The following count against the Annual Allowance:

1. any contributions made to a registered pension scheme that attract tax relief, plus
2. any contributions made by another individual on the member's behalf (eg a parent or grandparent on behalf of a child or grandchild, plus
3. any contributions made by the employer on behalf of the member

Note: The contributions made to a scheme in a tax year will not necessarily count towards the Annual Allowance for that tax year. Some may count towards the next tax year's allowance (see comments under 'pension input period' below).

For an active member of an occupational pension scheme, there is a different measure for valuing the effective level of pension savings attributable for Annual Allowance purposes. The administrator of that scheme will be able to provide details.

What happens if the Annual Allowance is breached in a tax year?

If the Annual Allowance is breached in any tax year the member will become personally liable to a charge on the excess. The tax due is calculated as follows. The amount of the excess pension savings is added to the amount of income they actually pay tax on. The amount of pension saving:

- over their higher rate limit will be taxed at 50 per cent
- over their basic rate limit but below their higher rate limit will be taxed at 40 per cent
- below their basic rate limit will be taxed at 20 per cent

The member is obliged to declare any liability to an Annual Allowance charge to HMRC through their self-assessment return.

A liability to an Annual Allowance charge does not mean that any relief granted (or due) on any contributions previously made is lost. There is no liability to a tax charge on such contributions, nor is there loss of any tax relief previously granted.

The ‘pension input period’

Contributions made to a scheme in a tax year will not necessarily count towards the Annual Allowance for that tax year. Under every scheme of which someone a member there will be what is called a ‘pension input period’.

Any contributions made in a ‘pension input period’ (other than any made that do not attract tax relief) count against the Annual Allowance for the tax year in which that period ends. This includes any contributions the employer makes on the member’s behalf in this period (whether or not the employer gets tax relief on those contributions).

Under the MW SIPP 2 the first ‘pension input period’ will normally end on 5th April following the date of the contribution and thereafter will run on a tax year basis.

The pension input period does not have to run on a tax year basis. For example, if the ‘pension input period’ started on 1st January 2012 and ran for the next 12 months, it means that the ‘pension input period’ would end on 31st December 2012, which is in the 2012/13 tax year. Therefore, every (relevant) contribution made in that calendar year period i.e. from 1st January 2012 to 31st December 2012, would count against the Annual Allowance for the 2012/13 tax year; none would count against the allowance for the 2011/12 tax year.

In this example, this means that any contributions made in the 2012 calendar year:

- by the member (or another individual on their behalf) where tax relief is due, and
- any employer of the member,

will all count towards the Annual Allowance for the 2012/13 tax year

Changing the ‘pension input period’

It is possible to change the ‘pension input period’. It is not possible to extend a ‘pension input period’ beyond 12 months or change a ‘pension input period’ twice in the same tax year (so that the member would end up with two periods ending in the same tax year).

The member may, for example, want to change the timing of this period to mirror:

- the ‘pension input period’ under any other scheme of which they are a member, or
- the company/business accounting period, or
- the scheme renewal timing

If the ‘pension input period’ is changed this will mean that not all the contributions made in each tax year will count against the Annual Allowance for that tax year; some will be counted against the following year’s Annual Allowance. However, the end date of the pension input period cannot be backdated.

Carry forward of unused tax relief

Any unused tax relief in the previous 3 years can be carried forward, provided that they were a member of a Registered Pension Scheme in the tax year for which relief is being carried forward. So if someone was in a Registered Pension Scheme in the 2010/11 tax year but contributed zero and they contributed £30,000 in 2011/12, they could contribute £120,000 in 2012/13 and get full tax relief at their marginal rate.

In determining any carried forward tax reliefs prior to 6.4.11, contributions are limited to £50,000. So if someone contributed £60,000 in 2010/11, they have no unused tax relief to carry forward - although their contribution was below the then Annual Allowance of £255,000, it exceeded £50,000.

What if someone is a member of another pension scheme?

If someone is an active member of another Registered Pension Scheme they will need to contact the Scheme Administrator to see what will count under that scheme towards the Annual Allowance in any particular tax year.

We do not give financial advice. nor do we advise on the suitability of a SIPP. No comments here are intended as such. The above information is based on our understanding of the legislation governing pensions at the time of writing. Before taking any action you should consult a qualified financial and/or tax adviser. Levels, bases of and reliefs from taxation may be subject to change.

This Newsletter is intended for professional advisors only, not members of the general public

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