CONTRIBUTIONS AND THE ANNUAL ALLOWANCE

Online links to further information are shown in underlined text below.

Summary

Contributions can be paid to a SIPP or SSAS by members and their employer. Full tax relief is given at the highest marginal rate on contributions, provided they are within certain limits set by the government from time to time. These are detailed below, but a summary of the conditions for tax relief are:

- Personal contributions must be within 100% of earnings and employer contributions must be reasonable for your position in the company
- Contributions can be paid at any time but no relief is available on contributions paid after age 75
- Contributions in excess of the government's *annual allowance* (or money purchase annual allowance or tapered annual allowance if these are applicable to you) will be subject to an annual allowance charge (see below)

There is no requirement to pay contributions to a SIPP or SSAS and they can be stopped, varied and re-started at any time. Contributions can be paid to more than one pension arrangement at the same time, subject to the overall limits.

Contributions are normally paid by cheque or standing order.

Annual Allowance

The Annual Allowance is the maximum addition to pension savings in each year which does not incur a tax charge. It applies to contributions into pension schemes (made personally by you or by your employer), and also to increases in the build up of benefits in defined benefit (or "final salary") type schemes. This note covers only the pension contribution aspect, i.e. the maximum pension contributions on which tax relief can be obtained.

The current standard annual allowance is £40,000 and, although contributions above this limit can be paid, no tax relief is available on the excess.

Money Purchase Annual Allowance

If you take an income under the new pension freedoms (Flexi-access or UFPLS), the annual allowance thereafter reduces to £4,000 for Money Purchase arrangements (known as Money Purchase Annual Allowance).

Tapered Annual Allowance

Pensions tax relief for higher earners is reduced from April 2016 with the introduction of the Tapered Annual Allowance. The standard annual allowance is reduced by £1 for each £2 of a person's *adjusted income* above £150,000 subject to an Annual Allowance floor of £10,000 minimum.

For example, if *adjusted income* is £170,000, the Annual Allowance reduces by £10,000 to £30,000. If *adjusted income* is £210,000 or more, the Annual Allowance has reduced to the minimum level of £10,000.

The principle is simple, but the complicated part is the way in which the *adjusted income* figure is calculated. The reduction in the Annual Allowance will be triggered if both of the following apply:

- *Adjusted income* is above £150,000
- *Threshold income* is above £110,000

Adjusted Income

This is:
Income for the year chargeable to income tax. This includes income from all sources, including things like dividends and property income
Plus: Any employee pension contributions deducted by the employer from gross pay
Plus: Any employer pension contributions (including any paid as a result of salary sacrifice)
Less: Any taxable lump sum death benefits received from someone else's pension scheme on or after 6 April 2016

Threshold Income

This is:
Income for the year chargeable to income tax, in the same way as for *adjusted income* above
Plus: Any income given up in exchange for pension contributions using salary sacrifice (or any similar arrangement) after 8 July 2015
Less: The gross amount of any personal pension contributions paid from net income, where the pension scheme reclaimed basic rate tax ("relief at source")
Less: Any taxable lump sum death benefits received from someone else's pension scheme on or after 6 April 2016

There are anti-avoidance measures to prevent people from manipulating their income to avoid triggering the reduced Annual Allowance.

Example

In the 2017/18 tax year, John has a salary of £100,000 and receives £30,000 of dividends. He pays £15,000 gross of personal contributions to his SIPP, which operates the relief at source method, and his employer also pays a pension contribution of £25,000.

His *adjusted income* is:
Salary of £100,000 + dividends of £30,000 + employer contribution of £25,000 = £155,000

His *threshold income* is:
Salary of £100,000 + dividends of £30,000 – personal contribution of £15,000 = £115,000

Adjusted income exceeds £150,000 and *threshold income* exceeds £110,000, so the reduced Annual Allowance is triggered. The excess of *adjusted income* above £150,000 is £5,000, so the standard Annual Allowance reduces by £2,500 to £37,500. John will not receive tax relief on the full £40,000 of pension contributions paid, unless he has "carry forward" available from a previous year (see below).

UK Relevant Earnings

Tax relief is given on contributions based on "UK relevant earnings" as defined by the government. Earnings for this purpose include UK salary, bonus, benefits-in-kind and self-employed earnings and profits, but not dividend or rental income.

If you have no UK relevant earnings then contributions of up to £3,600 p.a. can still be paid and receive tax relief. If you become non-resident by moving out of the UK, these contributions can continue to be paid for a further 5 tax years.

Personal Contributions

You qualify for full personal tax relief on personal contributions of up to 100% of your UK relevant earnings.

You pay personal contributions to SIPPs net of basic rate tax relief, and we then reclaim the basic rate tax relief from HMRC. For example, if you pay in £80 net, we reclaim £20 on your behalf and the scheme then has £100. It can take six to ten weeks for the tax reclaim to be paid, and this needs to be borne in mind when planning any investments. Any higher rate tax relief can be claimed through your annual self-assessment return.

Personal contributions to a SSAS can either be paid net of relief as above, or gross through the employer's PAYE system.

Employer Contributions

If you are employed, your employer can pay gross contributions to your SIPP or SSAS and receive corporation tax relief. To qualify for tax relief, the contribution must be wholly and exclusively for the purpose of the business, i.e. not simply for tax benefits.

HMRC provides guidance on what would be an acceptable contribution for tax relief, but there are no fixed rules and it is down to the local Inspector to make a decision. In practice if your remuneration package (salary, bonus, pension contribution) is at a commercial level taking account of your role in the company and its trading position, relief should be given. By contrast, if your salary is less than a commercial rate and the pension contribution is artificially inflated, this is less likely to be allowable. More detailed guidance is given in HMRC's Business Income Manual (section BIM46000 onwards).

If the employer's total contribution to a pension scheme:

- Exceeds 210% of the contribution paid in the previous accounting period, and

- The amount of the contribution over and above 110% of the contribution in the previous period is £500,000

then tax relief on the excess contribution will normally be spread forward over two or more accounting periods.

Carry Forward Rules

You are able to carry forward any unused annual allowance within the annual limit from the previous three tax years and pay top-up contributions in respect of the unused allowance. Prior to 6th April 2014 the Annual Allowance was £50,000.

For example, if you had not taken benefits by flexi-access and paid a contribution of £20,000 in the year ending 5 April 2017, you have £20,000 unused annual allowance for that year, and you could pay a carried-forward contribution of £20,000 in 2017/2018, on top of your normal contribution for that year. Note that to qualify for carry forward, you must have been a member of a pension scheme in the year you are carrying forward.

The annual allowance for the current tax year must be fully utilised before contributions can be applied to unused annual allowance carried forward.

Protection Against the Lifetime Allowance

You may have applied for one of the various types of Protection on your pension funds if you felt that they would exceed the Lifetime Allowance (see our Lifetime Allowance notes). A condition of most types of Protection is that you must not pay any more pension contributions, otherwise protection will be lost.

Pension Input Period

The "Pension Input Period" is the period in which the Annual Allowance applies. With effect from 5 April 2016 all Pension Input Periods follow the tax year, but it has been possible historically to vary the Pension Input Period to allow two year's worth of Annual Allowances to be contributed in a single tax year.

Other Requirements

You must supply evidence of the source of wealth from which contributions are being paid, for example a P60 to confirm earnings or a statement confirming the sale of an investment. If a financial adviser has set up the pension scheme for you, they will confirm to us that they have obtained this information; otherwise you should supply it directly to us.

We accept contributions on the basis that you are responsible for ensuring that they are within the various limits set out above and have carried out the necessary checks. Excess contributions can be refunded, but only within the same tax year. If we have reclaimed tax on a contribution and it turns out tax relief is not available, this tax must be returned to HMRC. Investments may need to be sold and charges may apply.

Curtis Banks Ltd

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