BRIEFING
15 JULY 2015

The July 2015 Pensions Budget Supplement

A. OVERVIEW

1. This paper summarises changes announced or confirmed by the Chancellor of the Exchequer on 8th July, 2015 that impact on pension schemes or are otherwise of interest.

2. The Summer Finance Bill 2015, containing legislation implementing the reduced annual allowance (see **B.3** and **B.4** below) and the reduction in the tax rate applicable to lump sum death benefits attributable to those aged 75 and over (see **B.5** below), was published on 15th July, 2015.

3. The Bill will progress only as far as Second Reading before summer recess begins on 21st July, 2015. The remaining stages will take place after Parliament returns on 7th September, 2015.

4. The July Budget documents are on the gov.uk website

B. PENSION SCHEMES

1. Reduction in lifetime allowance from 6th April, 2016

The reduction in the lifetime allowance ("**LTA**") from £1.25 million to £1 million, announced in the March, 2015 Budget, is confirmed. From 6th April, 2018, the LTA will be indexed in line with increases in the CPI.

Fixed and individual protection regimes will be introduced alongside the reduction. The legislation implementing the reduction will be in the Finance Bill 2016 (*Budget Report para 2.82*)

2. Removal of restrictions on buying and selling annuities

The March 2015 Budget Statement announced that individuals already receiving income from an annuity would be able to assign their annuity income stream to a third party buyer in exchange for a lump sum or an alternative retirement product, provided that the original annuity provider agreed to the transaction. A call for evidence published alongside the Budget gave further details.

The change was intended to take effect on 6th April, 2016. The Government has announced that, following consultation, implementation will be delayed until 2017. Further plans for introducing the measure will be set out "*in the Autumn*" (*Budget Report para 2.81*).

3. Reduced annual allowance for high earners

The Budget contained further detail on the Conservatives' manifesto pledge to reduce tax relief on pension contributions for those with incomes above £150,000 by tapering away their annual allowance to a minimum of £10,000.

The change will take effect on 6th April, 2016. The legislation is in the Summer Finance Bill 2015.

An HMRC tax information and impact note ("**TIIN**") contains the following additional details:

– the taper will apply to an individual with annual "**adjusted income**" of more than £150,000. "Adjusted income" includes the value of pension contributions made by the individual or on his behalf. The Government

says that this is to prevent individuals avoiding the taper by use of salary sacrifice.

- employer contributions to money purchase arrangements are added back when testing the £150,000 threshold.

- the value of employer contributions in respect of a defined benefit or cash balance arrangement for a tax year will be the pension input amount for the arrangement for annual allowance purposes, less the total of any member contributions.

- there will be an income floor of £110,000 (the "**threshold income**"). The taper will not apply unless the individual's income **excluding pension contributions** exceeds that amount. This is intended to ensure lower paid individuals are not affected by the taper by virtue of one-off spikes in employer pension contributions. But any employment income given up in exchange for pension contributions under a salary sacrifice arrangement entered into on or after 9th July, 2015 will be included in an individual's threshold income.

  Comment: It is not clear whether this will affect individuals who join an existing salary sacrifice arrangement on or after that date.

- the taper will reduce an individual's annual allowance by £1 for every £2 that his adjusted income exceeds £150,000 subject to a maximum reduction of £30,000. An individual with an adjusted income of £210,000 or more will have an annual allowance of £10,000.

- where an individual is subject to the money purchase annual allowance through having flexibly accessed his pension rights, the alternative annual allowance (that applies to non-money purchase pension saving and that is currently limited to £30,000) will be reduced by £1 for every £2 by which the individual's income exceeds £150,000, subject to a maximum reduction of £30,000. So an individual with adjusted income of £210,000 who is subject to the money purchase annual allowance will have no alternative annual allowance available.

- an individual affected by the taper will still be able to carry forward unused annual allowance on the existing basis (although restricted to the unused tapered annual allowance).

4. Alignment of PIPs

To facilitate the annual allowance taper for high earners (see **B.3** above), the Government is to introduce legislation to align pension input periods ("**PIPs**") with the tax year with immediate effect from 8th July, 2015. A PIP that was open on 8th July, 2015 closed on that date. The next PIP runs from 9th July, 2015 to 5th April, 2016. All subsequent PIPs will match the tax year.

Comment: This means that all arrangements in existence on 8th July, 2015 will have 2 or 3 PIPs ending in the 2015/2016 tax year, depending on the start date of the open input period.

Transitional measures apply so as to give individuals an £80,000 annual allowance for 2015/16, on the basis that, for savings made between 9th July, 2015 and 5th April, 2016, the allowance is limited to £40,000. Overall, the 2015/16 tax year will be split into two "mini" tax years (the "**pre-alignment tax year**" and the "**post-alignment tax year**"). There are special rules for applying this mechanism to DB and cash balance schemes.

Carry forward will continue to apply as currently i.e. any unused annual allowance from the 3 previous tax years can be carried forward to the current tax year. But, for 2015/2016, the 2 "mini" tax years will be treated as one tax year for the purpose of calculating from which years annual allowance can be carried forward.

For the pre-alignment tax year, carry forward will be available for unused annual allowance from 2012/13, 2013/14 and 2014/15, as at present.

For the post-alignment tax year, carry forward will be available for unused annual allowance from those same years plus the limited carry forward (up to £40,000) from the pre-alignment tax year.

For 2016/17 carry forward will be available from 2013/14, 2014/15 and the pre-alignment tax year i.e. it will not be possible to carry forward unused annual allowance from the post-alignment tax year.

Further details of the transitional arrangements, including carry forward, are in draft guidance published by HMRC.

According to the draft guidance, there are to be no new reporting requirements on scheme administrators arising from the transitional year, so pension saving statements for 2015/16 will have to be provided to members by 6th October, 2016 regardless of which "mini" tax year they relate to.

The draft guidance also states that HMRC will consider "at a later stage" whether the regime can be simplified by removing the concept of PIPs altogether.

5. **Taxation of lump sum death benefits**

As announced in the Autumn Statement 2014, the Government is to reduce the 45% tax rate that applies on lump sums paid from pension assets of an individual who dies aged 75 and over. From 6th April, 2016 the recipient will be subject to tax at his marginal rate of income tax. The legislation is to be contained in the Summer Finance Bill 2015.

According to HMRC's TIIN on the subject, where the recipient is a trust or company without a marginal tax rate, the 45% rate will continue to apply.

6. **Access to Pension Wise**

The Government says it is extending access to the Pension Wise service to those aged 50 and over. The service is currently available only to those aged 55 and over *(Budget Report para 2.85)*.

7. **Reform of pensions tax relief**

HM Treasury has published a consultation paper on a possible reform of pensions tax relief.

The paper does not put forward any particular options (although it raises the possibility of moving from the current "EET" (exempt, exempt, taxed) system to a "TEE" (taxed, exempt, exempt) system, as currently applies to ISAs).

The consultation paper, on which responses are invited by 30th September, 2015, is here.

8. **Equitable Life**

The Equitable Life Payment Scheme is to close to new claims on 31st December, 2015 (*Budget Report para 2.86*).

9. **Unfunded Employer Financed Retirement Benefit Schemes ("EFRBS")**

The Government is to consult on tackling the use of unfunded EFRBS to obtain a tax advantage in relation to remuneration (*Budget Report para 2.80*). No further information is available.

10. **Salary sacrifice schemes**

The Budget Statement observes that, as the cost to the taxpayer from salary sacrifice arrangements is rising, the Government is actively to monitor their growth and the effect on tax receipts (*Budget Report para 1.197*)

C. TAX CHANGES

1. **Income tax rates and bands 2015/2016 and 2016/2017**

The Chancellor confirmed that the main rates of income tax, national insurance and VAT will not be increased for the duration of this Government. The Government will legislate to ensure that rates remain unchanged for the next 5 years.

The income tax personal allowance rises from £10,600 (2015/2016) to £11,000 for 2016/2017 and £11,200 for 2017/2018. The basic rate limit increases from £31,785 (2015/2016) to £32,000 for 2016/2017 and £32,400 for 2017/2018. As a result the higher rate threshold will be £43,000 in 2016/2017 and £43,600 in 2017/2018.

The following rates and bands apply for the tax year 2015/2016 and 2016/2017:

	RATE OF TAX (%)		TAXABLE INCOME (£)*		
	2015/16	2016/17	2015/16	2016/17	2017/18
Basic	20	20	0 – 31,785	0 – 32,000	0 – 32,400
Higher	40	40	31,786 – 150,000	32,001 – 150,000	32,401 – 150,000
Additional	45	45	Over 150,000	Over 150,000	Over 150,000

** Taxable income is defined as gross income for tax purposes less those allowances and reliefs available at the taxpayer's marginal rate.*

Note: *For 2015/16 a spouse or civil partner who is not liable to income tax above the basic rate is able to transfer up to £1,060 of their personal allowance to their spouse/civil partner.*

2. Dividend income

From 6th April, 2016 the 10% dividend tax credit is abolished. Individuals will instead have a Dividend Tax Allowance of £5,000 a year. The new rates of tax on dividend income above this allowance will be:

- 7.5% for dividends otherwise taxable at the 20% basic rate,
- 32.5% for dividends otherwise taxable at the 40% higher rate, and
- 38.1% for dividends otherwise taxable at the 45% additional rate.

The legislation will be in the Finance Bill 2016 (*Budget Report para 2.57*).

3. Savings income

Currently, savings income (other than dividend income) up to £5,000 (the "starting rate limit") is exempt from tax. Savings income between the starting rate limit and the higher rate band is taxed at 20%.

As announced in the March 2015 Budget, a Personal Savings Allowance, to exempt from tax up to £1,000 of savings income for a basic rate taxpayer, and up £500 for a higher rate taxpayer, will be introduced on 6th April, 2016. The allowance will not be available to additional rate taxpayers. The legislation will be in the Finance Bill 2016 *(Budget Report para 2.57)*.

4. Inheritance Tax

The nil rate band, previously frozen at £325,000 until 6th April, 2018, will now remain frozen until 6th April, 2021.

For deaths on or after 6th April, 2017, there will be an additional nil-rate band (£100,000 in 2017/18, gradually increasing to £175,000 in 2020/21) where a residence is passed on death to "direct descendants". Any unused amount will transfer to a surviving spouse or civil partner. There will be a tapered withdrawal of the additional nil-rate band for estates with a net value of more than £2 million *(Budget Report para 2.88)*.

5. ISA withdrawals

The Government has confirmed that regulations will be introduced "*in the Autumn of 2015*" to enable ISA savers to withdraw and replace money from cash ISAs (and cash from stocks and shares ISAs) without it counting towards their ISA subscription limit for that year *(Budget Report para 2.78)*.

6. Non-domiciled individuals

The Chancellor announced major changes to the taxation of non-UK domiciled individuals ("**non-doms**") (*Budget Report para 2.63*). The detail is in an HMRC technical bulletin.

Currently, where a non-dom claims the remittance basis so that foreign income and gains that are not "remitted" in the UK are not taxed here, a remittance basis charge applies for each tax year, on a sliding scale depending on the number of years during which the non-dom has been UK resident. The maximum is £90,000 a year for individuals who have been UK resident for 17 out of the past 20 years.

From 6th April, 2017, non-doms who have been UK resident for more than 15 of the past 20 years will be deemed UK domiciled for all tax purposes. They will no longer be able to use the remittance basis of taxation; UK income tax and CGT will apply to worldwide income and gains on an arising basis.

Further, once an individual has become deemed UK domiciled, they will be liable to inheritance tax ("**IHT**") on their worldwide assets rather than on their UK situate assets.

So far as relinquishing a deemed UK domicile is concerned, currently an individual who is deemed domiciled ceases to be such once they are non-UK resident for 4 complete tax years. With effect from 6th April, 2017, this will increase to 5 complete tax years.

Individuals with a UK domicile of origin who leave the UK currently remain UK deemed domiciled for IHT purposes for at least 3 years after they have formed the intention to settle permanently overseas. This period is to be increased from 3 years to 5 years for individuals who have been UK resident for at least 15 tax years prior to leaving the UK.

Individuals with a UK domicile of origin who have acquired a foreign domicile of choice and who return to the UK to take up tax residency will be treated as UK domiciled individuals as soon as they become UK resident.

Note: The new rules will apply from 6th April, 2017 regardless of when someone arrived in the UK. There will be no special grandfathering rules for those already in the UK. For those who leave the UK before 6th April, 2015, but who would be deemed domiciled under the 15 year rule on 6th April, 2017, the existing rules will apply.

The Government is to consult on the detail of the rules after the summer recess. The legislation will be in the Finance Bill 2016

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