October 2011

PENSION SAVING IN EXCESS OF THE ANNUAL ALLOWANCE

Pensions/Employment/Taxation and Benefits

THE NEW ANNUAL ALLOWANCE OF £50,000 MEANS THAT REGISTERED PENSION PLANS MAY NO LONGER PROVIDE THE COMPLETE RETIREMENT SOLUTION FOR HIGH EARNERS. SUBJECT TO "DISGUISED REMUNERATION" RULES, UNREGISTERED PENSION ARRANGEMENTS MAY HOWEVER PROVIDE AN ATTRACTIVE ALTERNATIVE.

The limits on saving through registered pension plans

Since 6 April 2011, saving through registered pension plans has been restricted by an annual allowance of £50,000 (plus unused allowance from the previous three tax years). From 6 April 2012 the limit on lifetime saving through registered pension plans – the lifetime allowance – will reduce to £1.5m (from £1.8m). Employers need to consider how they will assist employees who are at or near these limits.

Some employers are looking to cap pension savings in registered pension plans to avoid breaching the new allowances. The question remains: what alternative pension provision will be offered to mitigate the employees' losses?

Unregistered pension plans

Employers can offer their employees additional or alternative pension provision through an unregistered pension plan. These arrangements (now known as Employer Financed Retirement Benefit Schemes or EFRBS) are subject to new disguised remuneration rules, but remain viable in some forms. Whilst the tax advantages of funded EFRBS have been withdrawn and the use of secured EFRBS curtailed, unfunded unsecured EFRBS remain viable.

An unfunded unsecured EFRBS deserves careful consideration when reviewing the options for employees who wish to accumulate high levels of pension savings.

The Finance Act 2011

The Finance Act 2011 has cut the amount of tax relieved pension savings that individuals can build up in registered pension plans to £50,000 per annum plus the unutilised portion of a £50,000 allowance from the previous three tax years. As mentioned above, the Finance Act 2011 provides for the reduction of the lifetime allowance to £1.5m from 6 April 2012.

The Finance Act 2011 has also introduced disguised remuneration rules whose ambit includes employer contributions into funded or secured EFRBS. Mechanically the disguised remuneration rules result in the employer incurring PAYE and NIC charges whenever the EFRBS allocates employer contributions to the employees, no matter how informally. In effect, an EFRBS of this kind is unlikely to be tax efficient.

However, HM Revenue and Customs have indicated in their published guidance that the disguised remuneration rules do not apply to unfunded unsecured EFRBS.

What is an unfunded unsecured EFRBS?

An unfunded unsecured EFRBS is a contractual promise from an employer to pay pension benefits to an employee as and when they fall due. They differ from traditional pension plans in that there is no money set aside to pay the pension or to provide security in respect of the payments.

The unfunded unsecured EFRBS commitment is likely to be accounted for as a liability on the employer's balance sheet. The employer will receive tax relief when the pension benefits are paid and the employee's tax treatment mirrors this.

The new landscape

Employers of individuals who are affected by the annual allowance and/or the lifetime allowance will have to navigate carefully through the new regulatory landscape. Alternatives to savings in registered pension plans include company share plans, tax favoured ISAs and VCT savings opportunities, or even giving the employee more cash. Unfunded unsecured EFRBS should also be on the menu of options when considering how to restructure benefit packages to make them more attractive to employees, whilst still falling within the boundaries created by the Finance Act 2011.

Opportunities also exist to help employees take advantage of a reduction in their marginal rate of income tax when they retire. Please see our separate publication entitled "Transitional Retirement Income Planning" (August 2011).

Further Information

For further information please contact one of the individuals below or your usual contact at Squire Sanders Hammonds.

Matthew Giles
Partner, Pensions
T: +44 (0)121 222 3296
E: matthew.giles@ssd.com

Lawrence Green
Consultant, Taxation and Benefits
T: +44 (0)121 222 3394
E: lawrence.green@ssd.com

Gerry Peyton
Director, HR Plus
T: +44 (0)20 7655 1792
E: gerry.peyton@ssd.com

Charles Frost
Partner, Employment
T: +44 (0)121 222 3224
E: charles.frost@ssd.com

Please note that the tax planning techniques outlined in this note are dependent on being properly implemented and should not be used without taking appropriate legal advice

These brief articles and summaries should not be applied to any particular set of facts without seeking legal advice. © Squire Sanders Hammonds 2011.

5480/08/11

If you do not wish to receive further legal updates or information about our products and services, please write to: Richard Green, Squire Sanders Hammonds, Freepost, 2 Park Lane, Leeds, LS3 2YY or email richard.green@ssd.com.

Squire Sanders Hammonds is the trade name of Squire, Sanders & Dempsey (UK) LLP, a Limited Liability Partnership registered in England and Wales with number OC 335584 and regulated by the Solicitors Regulation Authority. Squire, Sanders & Dempsey (UK) LLP, is part of the international legal practice Squire, Sanders & Dempsey which operates worldwide through a number of separate legal entities. Please visit www.ssd.com for more information.

Lexcel Practice Management Standard Law Society Accredited

INVESTORS IN PEOPLE