

THE PRE-BUDGET REPORT - PENSIONS

Contribution limits

In times when investment prospects are uncertain and returns are low, it is more important than ever to maximise tax-efficiency; and as the tax year draws to a close, consideration should be given to pension contributions.

Notice was given in the Chancellor's pre-Budget report of the Government's intention to freeze pension contribution limits, but for most people these are still generous and continue to include higher-rate tax relief, despite periodic suggestions that this might be withdrawn.

Contributions are subject to an annual allowance which currently stands at £235,000 and will increase to £245,000 in the next tax year and to £255,000 in the tax year 2010/11, after which it will be frozen for at least five years.

It is in fact possible to use up to two years' annual allowances in one tax year, so that in the year ending 5 April 2009 a total of £480,000 could be invested and higher rate tax relief claimed of £192,000. However, this type of planning requires specialist advice.

In addition to the annual allowance there is a lifetime allowance, which caps the value of pension funds from which benefits which can be drawn tax-efficiently. This currently stands at £1.65m and will rise to £1.8m in 2010/11, when it also will be frozen until at least 2015/16.

Protection For Pensions

When the annual and lifetime limits for pensions were introduced in 2006, provision was made to enable individuals who could be affected by the limits to protect the funds they had already built up.

5 April 2009 is the latest date on which application can be made to HM Revenue & Customs for protection, and failure to apply could result in significant tax charges.

Anyone who realises pension benefits where the combined fund values are in excess of the lifetime allowance will suffer a penalty.

Where such excess benefits are in the form of capital they will be subjected to a tax charge of 55%. If the excess is taken in the form of income, the tax charge will be 25% followed by the usual charge to income tax.

For members of defined benefit occupational schemes, the test will not arise until the scheme benefits are crystallised on retirement, but registration for protection should be made immediately.

Salary Sacrifice

Another change impacting pension planning is the increase in the upper earnings limit for National Insurance contributions. This exceeds the increase in the limit at which higher rate income tax bites.

The result is that those earning more than £43,888 in 2009/10 will pay 11% NI on a greater proportion of their income. At present the upper threshold for 11% employee NI contributions is £40,040. The effect will be exacerbated from 2011, when the rate of NI will increase to 11.5%.

For employees, a solution may be to enter into a salary sacrifice agreement with the employer, balanced by a matching employer pension contribution, so as to remove from the NI charge the salary which has been sacrificed.

More generous companies may also add the Employers NI saving, 12.8% of the salary given up, meaning that in total an additional 23.8% is contributed to pension as compared to the employee making the same level of contribution personally.

Carrying back losses

Small companies may be able to benefit from the concession which permits losses to be carried back for more than the single year, which has applied until now.

Losses of unlimited size can be carried back for one year, but it is now permitted to carry back losses of up to £50,000 for up to three years. So tax which has already been paid can be reclaimed provided that a loss is made in the current year – which can easily be arranged by for example paying a large pension contribution.



The concession only applies to accounting periods ending between 24 November 2008 and 23 November 2009, so companies whose accounting period ends on 31 March will need to act quickly.

Increased State Pension

In order to qualify for a full State pension it is necessary to have paid NI contributions for at least 39 years (reducing to 30 years for people who retire after 2010). However, those with a shorter contribution record are able to buy extra years.

The cost per extra year is currently £421.20, but with effect from April 2009 it will increase to £626.60 – a rise of 48.7%! So there is much to be said for acting before the increase takes effect.

Those who are uncertain as to their contribution record can obtain a forecast from the Pension Service, part of the Department for Work and Pensions.

Higher Rate Income Tax

How interesting to read Lord Healey criticising the proposed introduction with effect from 2011/12 of a 45% tax rate for incomes over £150,000 p.a. It was he who as Chancellor Denis Healey in the early 1970s vowed at a Labour Party conference to tax the "rich" "until the pips squeaked".

On mature reflection Lord Healey regards such measures as a sop to the Left which has the negative effect of discouraging initiative and exacerbating the brain drain.

February 2009



No responsibility can be accepted for the accuracy of the information in this newsletter and no action should be taken in reliance on it without advice.
Please remember that past performance is not necessarily a guide to future returns.
The value of units and the income from them may fall, as well as rise. Investors may not get back the amount originally invested