TAXREP 13/10 IMPLEMENTING THE RESTRICTION OF PENSIONS TAX RELIEF

Memorandum of comment submitted in March 2010 by the ICAEW, in response to the consultation paper, Implementing the restriction of pensions tax relief, published in December 2009.

Contents **Paragraph**

Introduction		1	
Who we are	2	-	4
Major points	5	-	11
Background to measures	12	-	16
General points – our concerns	17	-	47
		-	
Responses to specific questions:		-	
Applying the restriction of the relief	48	-	64
Valuing the defined benefit contribution	65	-	74
Delivering the restriction of the relief	75	-	111
		-	
The Tax Faculty's ten tenets for a better tax system		Appendix 1	
Comments made during the passage of Finance Act 2004		Appendix 2	

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INTRODUCTION

1. The ICAEW welcomes the opportunity to comment on the consultation paper *Implementing the restriction of pensions tax relief* published by HM Treasury and HM Customs & Excise.

WHO WE ARE

2. The ICAEW operates under a Royal Charter, working in the public interest. Its regulation of its members, in particular its responsibilities in respect of auditors, is overseen by the Financial Reporting Council. As a world leading professional accountancy body, we provide leadership and practical support to over 134,000 members in more than 160 countries, working with governments, regulators and industry in order to ensure the highest standards are maintained. We are a founding member of the Global Accounting Alliance with over 775,000 members worldwide.

3. Our members provide financial knowledge and guidance based on the highest technical and ethical standards. They are trained to challenge people and organisations to think and act differently, to provide clarity and rigour, and so help create and sustain prosperity. We ensure these skills are constantly developed, recognised and valued.

4. The Tax Faculty is the focus for tax within the ICAEW. It is responsible for technical tax submissions on behalf of the Institute as a whole and it also provides various tax services including the monthly newsletter 'TAXline' to more than 11,000 members of the Institute who pay an additional subscription, and a free weekly newswire

MAJOR POINTS

Areas of particular concern and note

5. We are very concerned about the effect that the government's decision to reduce pensions tax relief for some high income individuals will have on pension savings generally. Only a few years after individuals were promised generous annual and lifetime tax relief on pension savings, coupled with a simpler regime, the government is now doing a U-turn on the amount of tax relief for contributions made by certain individuals. Coming so soon after the A day changes, this decision undermines confidence in pensions as a savings vehicle for retirement. Furthermore its throws severe doubt on the value and accuracy of the figures and projections on which the government is basing its fiscal and taxation decisions (paras 28 to 33).

6. The complexity of the provisions means that many will not be able to understand easily the effect on them of the provisions. We believe that more detailed consideration should have been given to other simpler options. Options such as restricting the annual and lifetime allowances, which although not specifically targeting the identified group, may have been simpler and less administratively burdensome to operate (paras 25 to 27).

7. Members are very concerned about the compliance burdens and associated costs which these rules will force on scheme adminstrators, employers and individuals. We are of the opinion that the impact assessment does not fully reflect these costs (para 36).

8. We are opposed to the retroactive effect of the charge where an individual's income increases unexpecedly during the tax year so that he or she will be faced with a tax charge when one had not been expected (paras 19 to 22).

9. The proposed requirement for employers to identify and request pension benefit statements for employees with earnings and benefits which in total exceed £130,000 should be dropped due to the significant administrative burden this would place on employers (paras 75 to 83). Instead, HMRC should target publicity at those who may be affected.

10. We believe that those in receipt of termination payments should have all, or a significant part, of such payments ignored in ascertaining gross income. Furthermore we believe that in such circumstances relief from the charge should also be granted on employer's additional contributions to pension schemes (paras 60 to 64).

11. Given that the quantum of the charge may be very high, and for some may be quite unexpected and due to circumstances outside their control, taxpayers affected by the charge should have access to a variety of ways of paying the amount due (paras 87 to 92).

BACKGROUND

Why the government is introducing these provisions

12. The cost of tax relief for pension savings has doubled over the last decade and the Government has identified that a disproportionate amount of tax relief on pension contributions is given to those on the highest incomes.

13. Given current economic conditions and to ensure that pensions tax relief remains affordable, the Chancellor announced in his 2009 budget speech that pension tax relief for those on the highest incomes would be restricted so that those with incomes of £180,000 and over would receive tax relief at the same rate as basic rate taxpayers. Those with incomes of between £150,000 and £180,000 will obtain the relief at a rate of between 40% and 20%, depending on the level of their income.

14. The new provisions will apply from 6 April 2011. In the intervening tax years (2009/10 and 2010/11), 'anti-forestalling' provisions were introduced so that those with high incomes who make increased contributions prior to April 2011 would not benefit from tax relief at the higher rates.

15. The government has stated that it wants the restriction to apply as fairly as possible to individuals in all types of pension and remuneration arrangements. The restriction will therefore apply to the value of all pension benefits funded, or to be funded, including employer contributions.

16. The government's stated aim is to have an appropriate balance between fairness and simplicity. The consultation seeks comments on various issues associated with the implementation of this policy.

GENERAL POINTS

Charge is complex and retroactive

17. Although the concept behind the provisions seems straightforward, in practice the provisions are complex. We believe that many of those who will be affected, particularly those in the income band £130,000 to £180,000 and those in defined benefit pension schemes will find the detailed proposals difficult to understand. Restricting pension relief in the way suggested means that there are numerous complications to deal with, both in the different definitions of income and the way in which the rules operate. Although the introduction of the 'floor' will assist some taxpayers in determining whether the provisions apply or not, it does in turn introduce further complexity and another definition of income.

18. The liability to the charge arises when income (as measured in different ways) passes certain thresholds for the tax year. There will then be a clawback of relief already given and/or no further relief granted. The charge will therefore be retroactive for many whose income in a tax year is more than expected or usual. We do not support a tax charge which will inevitably give rise to uncertainty for many taxpayers. We are particularly concerned about the difficulty some taxpayers will have in ascertaining the approximate level of the tax charge during the tax year so that they can put aside funds to pay the charge. This difficulty will apply predominantly to those in defined benefit schemes.

19. One issue which particularly concerns us is that the new regime will introduce unexpected tax charges for many individuals. Some taxpayers will know with reasonable accuracy that their total income for a given tax year is likely to be in excess of £150,000, and will have made pension contributions in the knowledge of the reduced tax relief they will obtain on these.

20. There will, however, be many who will not know their total income until after the end of the tax year and may have been making pension contributions in the expectation that they would receive tax relief at 40% and will have budgeted accordingly. This category will include self-employed individuals and partners whose profits tend to fluctuate from year to year and some employees. The self-employed and partners in particular will not be able to ascertain their taxable profits until after the accounting period end, which often coincides with the tax year end. It may take several months to calculate the quantum of profits which in turn means that once the charge has been calculated, there is less time to arrange payment.

21. There is also a significant risk that some individuals who will be subject to the pensions relief restriction will not be aware of this because their tax affairs are usually very straightforward or because their income is not usually 'high'. Those on fluctuating incomes could have very different after-tax incomes from year to year depending on which side of the thresholds their income falls in a given year. This makes financial planning difficult, uncertain and stressful.

22. This issue of uncertainty is recognised in the consultation document in the statement (para 3.25) that individuals may have made pension contributions expecting one tax treatment only to have another apply due to circumstances beyond their control.

23. Members have commented that the charge on contributions made to defined benefit schemes is particularly harsh because the employee will have been given full tax relief at source, arranged their financial affairs according to their remaining net income and simply will not have the cash to pay the additional charge. The situation is quite different from other benefits such as medical benefit where the tax charge is relatively small and may well be collected through PAYE.

24. We are pleased to note that the cliff-edge effect inherent in the anti-forestalling provisions will be mitigated when the new provisions are introduced by applying a taper to the level of the relief. However, the taper provisions may be difficult to understand and to apply in practice. Although this will add to the complexity of the provisions, this would appear to be justified in the circumstances.

More thought should have been given to other options

25. We understand that the government wanted to limit the amount of relief being given to those on the highest incomes. In addition, in the interests of fairness and recognising the considerable value to employees of pension provision funded by employers, it also wanted to include employer-funded pensions in the provisions. This aim inevitably results in complex provisions. In our view, taking into account the extreme complexity and additional administration burdens which the government's proposals and aims cause we believe that the government should have given more thought to other ways of limiting the amount of tax relief being given for pension savings.

26. Although we recognise that other options may not target the relief in exactly the way desired, we believe that more detailed consideration should have been given to alternative, and very much simpler, methods of restricting pensions relief such as substantially reducing the amount of the annual allowance (which is considered by many to be generous) or limiting the amount of relief according to fixed monetary amounts, perhaps given in bands based on age. The latter solution would have the very considerable advantage that individuals would be able to understand their tax position at the beginning of the tax year and plan accordingly. There is a precedent in the tax relief given on venture capital trust investments so the concept of granting tax relief at a different or limited rate has been tried and tested.

27. We appreciate that applying monetary caps for defined benefit schemes would inevitably be more difficult in practice than for defined contribution schemes and this issue would need detailed consideration. Options might include allowing employees to pay a lower level of contributions with corresponding reduction in benefits or to remain in the scheme at the existing level in the full knowledge of the level of the tax charge as the contributions are made. The former would involve pension schemes in considerable extra work and is therefore probably not practical. The charge on the employer contributions is more difficult to address.

Long term nature of pension savings and loss of certainty

28. As noted in previous submissions on pensions anti-forestalling (TAXREPs 29/09 and 32/09), pensions are a long term commitment. The over-riding aim of pensions tax relief is to encourage individuals to make this commitment and to save for their retirement. Although the proposed measure affects only those on the highest incomes, it will inevitably affect the way in which those on lower incomes will view pension savings.

29. Individuals may not now be prepared to commit to pension savings because they no longer believe that the framework within which they are making contributions will remain unchanged during the term of the investment. Bringing in this change so soon after 'A day', when pension savers were promised a certain future framework (see Appendix 2), coupled with the volatility of the stock markets means that individuals are now losing confidence in pensions as a method of saving for retirement.

30. For example, members have told us that following A Day with the introduction of the lifetime allowance and the annual allowance some individuals had deferred their retirement planning until, say, the last 10 years of their working life content in the knowledge that they had been given promised certainty for the future and would be able to make higher contributions at that time. This plan has been frustrated by the introduction of anti forestalling rules and also the proposed reduction in tax relief.

31. The removal of the higher rates of relief, and more particularly the additional charge to be made in respect of employer contributions, is likely to change many individuals' approach to pension savings. Many high earners may now take the view that they do not wish to use pension schemes for saving for their retirement because the current net cost of potential future and uncertain benefits is not sufficiently attractive to take the risk.

32. In particular, many individuals will be obtaining tax relief at only 20% on pension contributions when the pension income they eventually receive will be taxed at 40%, and perhaps even 50%.

33. It is very disappointing that the government was not able to predict a few years ago at the time of pensions simplification that the cost of its measures would be too high in the near future. It also throws into doubt the value of affirmations made by the government about its commitment to continuing with tax relief on pensions when the financial information on which it will be basing its decisions seems to be unreliable.

Costs of implementing the policy

34. Members have expressed considerable concerns about the costs of implementing the policy. There will be additional costs for individuals, employers, scheme administrators and scheme trustees. We understand that these costs are likely to be significant for defined benefit schemes and less onerous, but nonetheless an additional cost, for defined contribution schemes.

35. Trustees of pension schemes are under a duty to act in the best interests of all members of the scheme. We are concerned that trustees of pension schemes will be in breach of their fiduciary duties if they bear the cost, directly or indirectly, of providing the necessary information to a few members because this cost will be to the detriment of all the scheme members. If this is the case, schemes are likely to want to take legal advice about their position. We recommend that HMRC takes generic advice on this issue and makes this advice available to all trustees of pension schemes so that each scheme individually does not have to bear the cost of the advice with may well run to several thousands of pounds.

36. Members are concerned about the extra work and costs which employers will incur in implementing the policy in the way proposed and that individuals will incur dealing with their tax returns. We have commented on this in further detail in paras 101 to 111 below.

37. It will be very important for unrepresented taxpayers to have clear guidance before the start of the 2011/12 tax year indicating what they need to do in order to calculate the charge and the timescales which they should allow. Furthermore HMRC should not rely only on individuals reading the guidance notes to the tax return in full or finding information on their website and should ensure suitably targeted information is made available. This is particularly important because the charges which may arise could be very large indeed. Taxpayers need to be aware of the charges, plan for them and include them in their self assessment so they do not risk interest, surcharges and high penalties.

38. Employers will inevitably be asked questions by employees. We recommend that HMRC produces an information leaflet for those affected or who think they may be affected. Leaflets similar in style and approach to the ones recently produced for employers of student loan borrowers and the student loan borrowers themselves would be helpful. This would reduce the amount of time employers will need to spend on questions from employees. We should be pleased to comment on such leaflets before they are finalised.

39. The main issue for individuals in defined benefit pension schemes is the valuation of the deemed benefit and how easy it will be to obtain an indication of the likely charge for a tax year. Many employees will be looking to their employers and pensions funds for this information during the tax year, in advance of getting final figures at the end of the tax year. This will inevitably result in costs for the funds and the employer, which are likely to be particularly high in the 2011/12 tax year, the first year the charge will apply.

Pension scheme collapse

40. A number of members have raised the issue of what happens when members have paid tax on employer contributions to pension schemes which subsequently collapse or do not pay out the expected benefits. This issue has not been addressed in the consultation document although it was raised in workshops.

41. This would clearly not be a common occurrence but it is a very real possibility and we believe that some form of relief should be available in such situations.

Availability of information for employees

42. Members have reported that information about items such as share option gains and termination payments does not always reach the employee, may not be clear to the employee, may be included on the P60 for the wrong tax year and is dealt with inconsistently from employer to employer. Given that the amounts involved are often very large and may well cause an individual to be within the new regime when they would usually not be, we should like HMRC to consider reviewing how these items are dealt with in practice and consider making changes so that taxpayers do not inadvertently overlook these items, resulting in penalties and interest.

All high earners do not receive a tax return

43. The statement at the beginning of paragraph 5.5 of the consultation document that 'all individuals with income of £100,000 or over are required to complete a self assessment return which means that all those affected by the restriction of pensions tax relief will already be within self assessment' is misleading. There will be many instances where individuals who are affected by this legislation will not 'already be within self assessment'.

44. The position as regards the issue of self assessment returns is as follows. Section 8 of the Taxes Management Act 1970 allows HMRC to issue a notice to file a return to anyone. As a matter of policy, HMRC issues these to those it believes are on incomes of £100,000 or over. Where individuals are not issued with a tax return, they are required to notify chargeability under s 7 TMA 1970 if s 7(3) does not apply. They would therefore be required to notify chargeability for example where they have a new source of untaxed income or are liable to the higher rates of tax. This means that individuals who have not have been issued with a tax return, may have an obligation to notify chargeability by 5 October after the tax year end. It will then be HMRC's decision whether or not to issue a self assessment tax return and if so, for what period.

45. There will therefore be instances where individuals who have not met the criteria in one tax year do meet them in the following year so the individual will not have received a self assessment return. There will also inevitably be instances where HMRC systems do not operate as expected or there is a delay in processing information, so HMRC may not yet have asked individuals who they would like to complete a self assessment return to do so.

46. We should therefore like to emphasise to HMRC that, when publicising the restriction of pensions tax relief, it needs to take account of the fact that not everyone who will be affected by these provisions will already be within self assessment

47. This in turn will mean that the costs associated with complying with the legislation may also be understated because each year there will be individuals who have not previously needed to complete a tax return who will be asked to do so as a result of their income increasing. For one-off increases, in the past such individuals may not have been asked to complete a self assessment return but will now have to do so in order to deal with the pensions tax charge.

RESPONSES TO SPECIFIC QUESTIONS

APPLYING THE RESTRICTION OF THE RELIEF

The Government welcomes views on the best balance to strike between the smoothness of the taper and simplicity for individuals.

48. Individuals whose income (including employer pension contributions) is between £150,000 and £180,000 will have the tax relief on their contributions reduced using a series of steps, referred to as 'taper'.

49. Our view is that the most appropriate way to deal with the taper would be to have a formula for calculating the relief. This would give an entirely smooth profile to the taper percentage. The taper percentage could operate in the same way as the reduction in age allowance and personal allowances does.

50. Although having a series of steps as proposed would mean that individuals could read the amount of relief from a table, it would make the calculation more difficult generally, particularly in computerised environments. Under our preferred option for taper, individuals should be able to estimate the approximate percentage relief due depending on where their income is between £150,000 and £180,000.

Given that the restriction of pensions tax relief for high-income individuals will apply over the tax year, the Government welcomes views on whether the pension input period for the purposes of assessment against the annual allowance should be brought in line with the tax year.

51. Each pension plan has a policy year that is determined either by the establishment of the scheme or a crystallisation event. This provides the basis of all trustee reporting to members as well as governing the amount of contributions that are paid in any one year, by employer or employee. Allowing schemes to have different year ends allows the workload for trustees to be spread while the burden of determining the correct tax treatment of contributions is passed to the taxpayer who needs to use the tax year.

52. In the interests of simplicity, it would seem logical for the pensions input period to be aligned with the tax year. However, such a change would undoubtedly have a significant impact on pension scheme administrators, resulting in bunching of work after the tax year end, an already busy time in the financial calendar. There would also be a one-off cost of change and ongoing costs associated with the workload peak.

53. Given that the current proposed changes are significant and it is likely that it will be at least a year or two before the practical effects of the amended rules will be fully understood, there seems little point in making further changes at this stage which are likely to have a major and unwelcome impact on pensions administration.

The Government welcomes views on any practical or administrative issues that may arise from applying the restriction of pensions tax relief to individuals on gross incomes of £150,000 and over who are members of overseas pension schemes and benefiting from UK tax relief.

54. It has to be recognised that members of overseas pension schemes will inevitably have considerable problems both obtaining the information which they need and obtaining it on a timely basis. Feedback from members indicates that there are relatively few of these schemes in existence but nonetheless those individuals who are part of the schemes will suffer far greater difficulties and costs determining their tax liabilities than members of UK schemes.

The Government welcomes views on the proposal to use the higher of gross income in the current or previous tax year for the purposes of assessing whether individuals are affected by the restriction of tax relief in the year that benefits are drawn.

55. It is our view that the proposal will add considerable and unnecessary complexity to already complex provisions. It doesn’t seem unreasonable for those whose income is reduced due to retirement to receive full tax relief for pension contributions made in the year of drawing benefits. We see no justification for looking at the previous year’s income to determine whether or not the threshold is met.

56. Furthermore we believe that such a provision would be extremely difficult to draft, operate and understand, both in general and particularly as regards the taper element of the charge.

57. We consider that the number of individuals who are likely to have income at the level which would fall above the threshold in one year and below it in another is likely to be extremely low and that those in that population who will have any scope to manipulate their income to advantage will be even smaller.

58. We are frequently advised that there are considerable costs associated with making changes to the SA100 tax return and associated guidance notes, calculation sheets and literature. We believe that this, coupled with the very low numbers likely to be able to use rules to their advantage, would not make such a provision sensible.

59. If the government is concerned about possible manipulation of pension inputs, remuneration packages and profits then it should use targeted provisions aimed at the mischief about which it has concerns.

The Government welcomes views on ways in which the impact on individuals affected by the restriction due to a redundancy payment of over £30,000 could be further mitigated without opening up scope for abuse.

60. We fully support the Government's view in paragraph 3.25 of the consultation document that the first £30,000 of a redundancy or other termination payment should be excluded from income for the purposes of both the £130,000 and £150,000 thresholds.

61. There are good arguments for the whole of any termination payment being excluded from income for these purposes because termination payments may be large and significantly distort the usual pattern of income. Depending on individual circumstances, the pensions relief restriction charge could then significantly reduce the amount of net termination payment which the ex-employee has to live on after loss of their employment.

62. We understand that HMRC views a termination payment as being in the nature of income, as it is to support the employee until he or she gets another job. This being the case, and if the whole of the termination payment is not to be excluded from income for the purposes of the charge, there must be strong arguments for having some sort of top-slicing relief for this income in these circumstances. However, we are reluctant to suggest this because it will increase complexity.

63. A simpler option for consideration is, where the £30,000 limit applies for income tax purposes, to increase the disregard for the purposes of the pension relief charge to a higher monetary amount such as £100,000. This would provide what is effectively a very crude form of top-slicing relief without the inherent complexity. It would almost certainly mean that those who would not have been liable to the pensions tax charge given their usual level of income would not be liable to it as a result of a lump sum paid on termination of their employment. Those who are already liable to the charge, will continue to be so liable and further consideration should be given to their situation.

64. We would like consideration to be given to a corresponding relief for employer top-ups to pension schemes on termination of employment.

VALUING THE DEFINED BENEFIT CONTRIBUTION

The Government welcomes views on how well the valuation methods meet the objectives of fairness and simplicity, and whether any other factors should be taken into consideration. Do stakeholders agree that (a two-way scale of) ARFs is the best approach for valuing the deemed contribution? If not, the Government welcomes views on what alternative method is preferable.

65. The valuation of defined benefit (DB) contributions will always be extremely difficult with so many factors which could be taken into account including age, sex, marital status, scheme financial security, scheme characteristics and normal retirement age.

66. Our members would find the flat factor approach the easiest to use and the easiest to explain to their clients. This approach would also be easiest for unrepresented taxpayers to use and should enable such taxpayers to make a reasonable estimate of their likely charge during or before the tax year. This alone is a strong factor in favour of using this straightforward approach.

67. Although, as explained in the consultation document, such an approach may lead to less fair outcomes between taxpayers in DB and defined contribution (DC) schemes, the differences being significant in certain circumstances, we question whether using the other methods proposed in the interests of fairness are justified. The additional costs associated with the more complex valuation methods would appear to place considerable additional burdens on scheme administrators and employers.

The Government welcomes views on whether a two-way ARFs scale is preferable to a one-way scale; which other influencing variables an ARFs scale should include in an average sense, bearing in mind the objectives of fairness and simplicity; whether there is any reason why cases where individuals have more than one NPA could not be treated using a two-way ARFs scale; whether the individual or the scheme should carry out the ARFs calculation to compute the deemed contribution; whether GAD should have a role in advising HM Treasury on setting and reviewing the scale; and how the scale should be reviewed, taking into account predictability and fairness.

If respondents favour the CETV approach, the Government welcomes their views on why the CETV methodology is appropriate given the Government's principles of fairness and simplicity; the best way to apply the CETV methodology to value the deemed contribution for the purposes of restricting tax relief; and whether market movements should be stripped out and, if so, how that should be done.

68. We have no comments on these two questions.

The Government welcomes views on whether there are any instances in which contributions or enhancements made to an individual's pension should not be subject to the restriction of pensions tax relief and why these exemptions are justified in the light of the Government's stated objective of fairness; and how these exemptions might best be crafted to avoid opening up scope for avoidance.

69. Our main concern here would be for those individuals who take early retirement as a result of injury, incapacity or illness. There are many precedents in both social security and tax legislation for treating these as special cases.

70. Where an individual has needed to draw pension benefits early as a result of illness, incapacity or injury causing them to be unable to work, the employer may make enhanced contributions to the scheme or the deemed benefit contribution on drawing unreduced pension may high in the tax year. In such cases, we believe that the enhancements or contributions should be ignored.

71. We understand that schemes will each have their own rules governing drawing pension benefits early in such cases. Where an individual has been granted early retirement on grounds of illness, incapacity or injury, in order to avoid possible avoidance, the legislation should indicate the circumstances in which the enhancements or contributions will be ignored.

72. We would also want HMRC to provide a clearance procedure so that individuals in these circumstances, which will inevitably be life-changing and worrying, will have certainty over the tax treatment of their contributions in the tax year in which the change takes place.

The Government welcomes views on the most appropriate treatment for DB employee contributions in a year when the deemed contribution is less than the value of the employee contribution.

73. No comment.

The Government welcomes views on any of the issues raised in Annexes C and D.

74. No comments.

DELIVERING THE RESTRICTION OF THE RELIEF

Requirement for employers to request pension benefit statements for some employees

75. We believe that the reason behind this proposed obligation (set out in para 5.10) for employers to request pension benefit statements on behalf of employees, where the employee's gross pay and benefits are £130,000 or above, is that the earlier the pension benefit information is requested, the more likely it is that the individual will be able to file his tax return on time with the correct figures. However, we do not support the requirement. It places an unwelcome additional administrative burden on employers, by creating extra work and costs at a time of the year when they are already very busy. We do not consider this to be justified and believe that the issue should be addressed in other ways.

76. Members advise us that most payroll packages they use will not be able to produce automatically a list identifying employees with either gross or taxable pay of £130,000 and over. This means that the process will almost certainly need to be a manual one and will therefore be time-consuming.

77. The requirement to consider benefits provided to employees in addition to gross pay is especially onerous because this information is generally held on different systems and in a different way to payroll information. In most cases, the two sets of information would first need to be combined and then tested against the income threshold.

78. Members have also raised with us their concerns about confidentiality and whether employers will, under existing data protection legislation, be able to write to pension schemes requesting the pension benefit statements.

79. Further, employees as a group may not all belong to the same pension schemes and may belong to several so the employer would need to ascertain the pension schemes involved, together with scheme administrator addresses and reference numbers for each employee. In practice in a business environment, obtaining and checking this information is likely to take at least one hour per employee each year except where the majority of employees belong to the same scheme where the time would reduce to about 10 to 20 minutes per additional employee per scheme.

80. Consideration also needs to be given to asking the pension fund managers to provide information in a standard format. Members report that pension information provided by different fund managers is different in content and layout which is likely to confuse taxpayers and may lead to taxpayers inserting incorrect figures on their returns resulting in the tax charge being over- or under-stated.

81. It is our view that it should be HMRC which identifies those individuals affected and not the employers. HMRC should have received the information about salary electronically from all employers in respect of earnings by 19 May following the tax year end. The P11D information should be provided by 5 July following the tax year. HMRC already has the information and the computer systems in place to identify those affected.

82. In view of the above issues, we consider that, if the government insists that the employer must identify employees in the way suggested, then the employer's obligation should be limited to the simpler requirement of:

- identifying those employees whose gross taxable income in the current employment as shown on the P60 for the immediately preceding tax year exceeds £130,000; and
- advising the employee of this fact and the need to obtain a pension benefit statement from their pension provider(s).

This will still require additional work to be undertaken by the employer, which we do not consider to be a justifiable burden to be placed on the employer, but will be less onerous.

83. Although the underlying reason for the requirement is laudable, we do not consider that the benefit to the individual is sufficiently high to warrant the extra costs to the employer which will result. We do not therefore consider it acceptable to require employers to do as is being suggested and believe that targeted publicity should be undertaken by HMRC instead.

The Government welcomes views on whether employers should automatically request that pension schemes provide pension benefit statements to any employee for whom they have previously asked for one.

84. As noted above we do not consider that employers should have this obligation at all.

85. If the employer has to request the statement for any employee for whom one has been requested previously, the pool of employees for whom a statement will be requested will increase every year. This will create continuing extra work checking the plan details, reference numbers and employee details.

86. We therefore do no believe that benefit statements should automatically be requested for all employees for whom one has been requested previously.

Do stakeholders agree that the Budget Payment Plan offers sufficient flexibility for those affected by the restriction of relief who wish to smooth payment of the tax liability across the year, paying a portion earlier than is legally required, if they wish to do so?

87. Feedback received has indicated that there is considerable concern among our members about how their clients will finance the tax due as a result of the restriction of pensions tax relief. The availability of the plan should be highlighted in any literature relating to the charge. However, members would like to see a range of options available to those affected because the charge will affect individuals who have a wide range of different circumstances, who became aware of the charge for a tax year at different stages during the annual cycle.

88. Members generally have little experience of how the Budget Payment Plan (BPP) works in practice because it is a relatively new arrangement. We recommend that the BPP should be given wider publicity, not only in the context of pensions tax relief reduction but also for settling tax liabilities generally. It is worth noting that comments have been received that, despite the direct debit guarantee, there is considerable resistance by some taxpayers to allowing HMRC direct debit access to their bank account.

89. The BPP could be a useful way for some of those affected by the provisions to make regular payments towards the liability but is unlikely to be appropriate for all, especially those who find out very late that they have a very large liability.

90. Given that interest will be charged on late payment of any tax owing, we believe that the instalment option should be made available to anyone for whom the charge is greater than £15,000 and not just to those for whom the scheme will not pay. Furthermore we should like to see the amount at which this option is available reduced to £5,000. This would be a significant amount of money for some individuals to find as a lump sum and it may not be in their best long-term interests to go the ‘scheme pays’ route and suffer a reduction in benefits as a result.

91. Where the charge is particularly large relative to the individual’s income, we should like HMRC to consider extending the instalment payment term to five rather than only three years.

92. In addition and where possible and appropriate, we should like the option to be available for taxpayers to opt to have some or all of the charge collected through PAYE. The current limit on the amount of tax which may be collected through K codes, the loss of personal allowances for those on incomes over £112,950, combined with the 50% tax rate being introduced, may mean that existing limits and criteria would need to be changed.

The Government welcomes views on its proposed approach to scheme pays and, in particular, whether the approach could be modified to minimise burdens, while delivering the same flexibility for individuals.

Is it appropriate to make scheme pays available only to those in defined benefit pension schemes, recognising that individuals in defined contribution schemes, whether

occupational or personal, have more scope to reduce contributions if they do not wish to incur the associated recovery charges?

93. While it may initially appear that only those in defined benefit pension schemes would incur unexpected charges, this is not the case There may be individuals whose income is normally below £130,000 but in one tax year is unexpectedly above £130,000, for example as a result of redundancy or an unexpected bonus. In such circumstances, they may have received higher rate tax relief through their PAYE code or the event may occur very late in the tax year so that they may not be able to adjust their pension contributions.

94. Therefore, in the interest of fairness, the scheme pays option should be available to all taxpayers affected by the charge.

Is it reasonable to allow individuals to only elect for a single scheme to pay in any given year, and for that scheme to pay only the portion of the charge relating to contributions or deemed contributions made to that scheme?

95. This is a difficult issue to address fairly without adding to administrative burdens and complexity. If the individual has a recovery charge which is potentially payable by more than one scheme, it would seem reasonable for the charge to be allocated pro-rata to those schemes.

96. However, if this is done and the individual is permitted to have only one of the schemes pay its proportionate share of the charge, the individual may have to raise funds to pay the rest of the charge. This would mean that such an individual is at a disadvantage as compared with those who have only one scheme.

For defined benefit schemes, given that the method and assumptions used to actuarially reduce the value of a pension could vary across schemes and could allow schemes to disadvantage members electing for the scheme to pay, is it appropriate to set parameters for calculating the actuarially fair offsetting reduction to a member's pension across all defined benefit schemes when implementing scheme pays, or to leave it to individual schemes' discretion?

97. We can see advantages and disadvantages to both options and hold no strong views either way.

Do stakeholders agree that it would be necessary to include an opt-out for the small minority of schemes that would be disproportionately affected, for example, by reference to a minimum level of funding?

98. Given the trustees' obligation to act in the best interests of the members of the scheme as a whole, there will undoubtedly be circumstances when schemes could not reasonably be expected to accept the liability for the payment of the recovery charge. Circumstances may include both lack of liquidity, for example where the main fund assets are in real estate, and low overall fund value such that payment of the charge would result in a high relative reduction in fund assets.

99. We therefore believe that an opt out should be included to cover situations such as these.

Do stakeholders consider that those with recovery charges exceeding £15,000 whose scheme is not able to pay the recovery charge should be allowed to spread payments over three years, with interest charged on the deferred element?

100. It is our view that this option should be made available to all and not just to those whose scheme is not able to pay the recovery charge. Furthermore we would like to see the level at which the charge may be spread reduced to, say, £10,000.

The Government welcomes views on the consultation Impact Assessment, attached as Annex E.

101. Members consider that the impact assessment seriously underestimates the costs of the change in policy.

102. As noted in para 43 the statement in para 33 of Annex E that the policy will not bring anyone new into self assessment is not entirely accurate. There will be a number of individuals each year who would not necessarily have already been included within self assessment, mainly where the increase in income was earnings subject to PAYE because there is usually a delay before these cases are identified.

103. The new requirements relating to net pay schemes appear to have been glossed over in para 35 of Annex E. It is not clear whether a re-design of the P60 is required (with consequent significant costs in terms of computer programming both by HMRC and software providers) or that the individual will need to obtain information from his employer direct.

104. In our view, in order that taxpayers and their agents can identify all the information needed to deal with the taxpayer's return accurately, it is inevitable that the P60 will need to be redesigned so that it clearly shows both gift aid payments and pension contributions made, what the employee's gross earnings are and how much the employer has contributed to an employee's private pension scheme. Such a change will inevitably introduce additional costs in computer programming and stationery for HMRC and employers.

105. It has been estimated by members that advising an individual client, whose income is such that they will be or may be affected by the new provisions, on their new tax obligations will take about 2 to 5 hours in the first year and a little less in subsequent years. For clients of smaller firms this would give an annual cost of about £125 to £350 and for those of larger firms the cost might be as much as £2,250 including VAT.

106. This comprises typically about 1.5 hours (range 1 hour to 3.5 hours depending on client and the projected income level) reviewing each potentially affected client's income and pension contributions, writing to (or meeting with) clients individually to explain how the new rules will apply to them, producing calculations tailored to their individual circumstances, providing advice on making provision to pay the tax due and what issues may affect this.

107. The time spent obtaining the details required for the tax return from the pension scheme (identifying schemes, references, addresses, writing a request, follow up and review) will depend on the number of schemes of which the taxpayer is a member, and typically take one and two hours per scheme. There will also be start up time costs associated with learning about the entry of the information onto the paper tax return or into a computerised package.

108. The clients who do not clearly have over £180,000 of income will need the most help and support to understand their position and the tax which might or will be due. This will need to be done prior to April 2011 for existing clients and as required for each new client and each client whose income increases so that they are potentially affected.

109. Where taxpayers are unreprsented, they are likely to want this information to be provided by HMRC together with assistance with working out how much they need to save for tax. We would like to see the cost of HMRC providing this information and support included in the impact assessment.

110. If HMRC does not intend to provide this level of support, more taxpayers will need to take paid-for advice so that they are able to meet their liabilities and obligations on a timely basis. The costs of this should be factored in.

111. We believe that a significant number of the 300,000 estimated to be affected by the policy are employed by the public sector (for example, doctors, senior civil servants, ministers etc). It therefore follows that costs relating to the implementation of the policy in respect of these individuals, including the costs of the pension schemes providing information to the individual, and the employer providing support, will fall on the public. It is not clear from the impact assessment to what extent these costs have been taken into account and if they have not been we believe that they should be.

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APPENDIX 1

The Tax Faculty's ten tenets for a better tax system

The tax system should be:

1. **Statutory**: tax legislation should be enacted by statute and subject to proper democratic scrutiny by Parliament.

2. **Certain**: in virtually all circumstances the application of the tax rules should be certain. It should not normally be necessary for anyone to resort to the courts in order to resolve how the rules operate in relation to his or her tax affairs.

3. **Simple**: the tax rules should aim to be simple, understandable and clear in their objectives.

4. **Easy to collect and to calculate**: a person's tax liability should be easy to calculate and straightforward and cheap to collect.

5. **Properly targeted**: when anti-avoidance legislation is passed, due regard should be had to maintaining the simplicity and certainty of the tax system by targeting it to close specific loopholes.

6. **Constant**: Changes to the underlying rules should be kept to a minimum. There should be a justifiable economic and/or social basis for any change to the tax rules and this justification should be made public and the underlying policy made clear.

7. **Subject to proper consultation**: other than in exceptional circumstances, the Government should allow adequate time for both the drafting of tax legislation and full consultation on it.

8. **Regularly reviewed**: the tax rules should be subject to a regular public review to determine their continuing relevance and whether their original justification has been realised. If a tax rule is no longer relevant, then it should be repealed.

9. **Fair and reasonable**: the revenue authorities have a duty to exercise their powers reasonably. There should be a right of appeal to an independent tribunal against all their decisions.

10. **Competitive**: tax rules and rates should be framed so as to encourage investment, capital and trade in and with the UK.

These are explained in more detail in our discussion document published in October 1999 as TAXGUIDE 4/99; see http://www.icaew.co.uk/taxfac/index.cfm?AUB=TB2I_43160,MNXI_43160

APPENDIX 2

Comments by the Financial Secretary during the passage of the Finance Act 2004

The FA 2004 provisions, which came into effect in 2006, were the result of considerable consultation and when the changes were being debated in the Public Bill Committee the then Financial Secretary to the Treasury noted that:

> 'We are sweeping away the existing rules and regulations and replacing them with a single regime for all tax-privileged pension saving. That represents a hugely positive step for those saving or looking to save towards their retirement.
>
> Simplification will introduce greater individual choice and flexibility. **For the first time, everyone will have the same opportunity to make tax-relieved pension savings over a lifetime. Our proposals will create a transparent, consistent and flexible system that is readily understood. That will make it easier for people to concentrate on things that matter, such as when and how much to save for their retirement, rather than on trying to understand anomalies between the different tax regimes**. [our emphasis]
>
> Simplification will reduce the administrative burdens and regulatory cost for pension schemes, their members, operators and sponsors, and will create opportunities for people to save more towards a pension and a retirement lump sum. The new rules will allow everyone to pay what they can afford when they can afford it.
>
> The pension simplification provisions represent the outcome of two formal consultations and extensive informal consultation. At every stage, we have had regard to the views of those who will be affected, whether individuals, employers or pension providers.
>
> The new regime will consist of two key controls: a lifetime allowance and an annual allowance for the amount of tax-relieved savings that can be made. It is important to recognise that the allowances will not prevent people from saving more in registered schemes if they wish to. The lifetime allowance will initially be set at £1.5 million and will rise to £1.8 million by 2010. The annual allowance will initially be set at £215,000 and will increase to £255,000 by 2010. Those allowances represent very generous levels of tax-relieved savings. They are far in excess of what 99 per cent. of the population currently save or are ever likely to. **However, they limit the amount of tax relief that very high earners can obtain, which is fair.** [our emphasis]'

These new (2006) provisions introduced both an annual allowance and a lifetime allowance so that that the tax relief obtained is restricted in a clear and transparent manner. Those taxpayers who took on board the message that the annual allowance was generous enough that they could make top up payments in later years now feel misled.