

Our reference:
February 2010

Title Initials Surname
Address 1
Address 2
Address 3
Address 4

Dear Title Surname

2009 Budget Implications

1. Purpose of this Information Note

The 2009 Budget introduced changes which may have an impact on your taxation and pension savings. This information note is intended to provide a summary of the key changes proposed by both the Chancellor's Budget on 22 April 2009 and the Pre-Budget Report on 9 December 2009. This is based on our current understanding of the law and consultation papers.

These are complex changes, and NILGOSC is not in a position to inform you definitively as to how you will be affected because it is only aware of the 'pensionable pay' element of your total income.

This note has been sent to a broad category of members to ensure that all those possibly affected are informed. You may find, after reading this note, that you are not affected by the changes.

This Information Note is laid out in three sections.

- **Summary of the Changes** - provides a brief overview of the changes.
- **Further Details of the Changes** - describes the specifics of each of the five changes. I have also added some definitions to some of the key terms used. The definitions of the key terms are set out at the end of each paragraph.
- **Next Steps** - provides information on some of the actions you may wish to take if you may be affected.

2. Summary of the changes

- From 6 April 2010, the personal tax allowance will be reduced for incomes over £100,000 per year. The full personal allowance will be lost if you earn over £112,950.
- From 6 April 2010, a 50% top-rate of income tax for incomes over £150,000 per year will be introduced.
- From 6 April 2011, higher rate tax relief for pension contributions will be restricted to 20% if your income is over £180,000 per year. Restrictions on higher rate tax will reduce from 50% to 20% depending on your income level between £150,000 and £180,000 per year. This may result in an annual tax charge to be paid through the self-assessment process at the end of each tax year.
- From 6 April 2011, there will be an increase of 1% to employer and employee National Insurance Contributions.
- New tax rules, called anti-forestalling rules, apply retrospectively with effect from 22 April 2009. These measures are aimed at preventing individuals increasing their normal pension savings to take advantage of the higher rate tax relief before the restrictions come into effect on 6 April 2011.

3. Further Details of the Changes

Please read this section carefully as there are varying definitions of income.

The definitions of the key terms are set out at the end of each paragraph.

3.1 Phased removal of personal tax allowance for individuals with taxable income above £100,000 from 6 April 2010

The full personal tax allowance for both this and the next tax year is £6,475. Your allowance may be lower than £6,475 based on your personal circumstances.

Each £2 of additional taxable income above £100,000 per year results in a £1 reduction in the personal allowance. Therefore a taxable income above £112,950 per year will result in the full loss of the personal allowance.

Those members earning between £100,000 and £112,950 in the 2009/10 tax year may wish to consider making Additional Voluntary Contributions (AVCs) to reduce their taxable income so as to retain their personal allowance therefore reducing the amount of tax paid. If your taxable income is between £100,000 and £112,950 any AVCs would effectively receive tax relief of 60%. This means for each £100 of AVCs paid £60 less tax would be payable.

Whether or not your tax liability is likely to change you may wish to consider Additional Voluntary Contributions (AVCs) as a way of reducing your tax payments. This may be beneficial to all higher rate taxpayers and even more so to those with overall income over £100,000. As part of this communication we have arranged with Prudential, our AVC provider, to offer individual meetings to explain how AVCs can reduce your tax bill and subsequently provide a tax free lump sum on retirement.

If you would like more detail you can book a meeting by e-mailing robert.stormonth@prudential.co.uk or by telephoning Robert on 01236 763486.

Definitions:

- *Personal tax allowance* is the amount you earn that is not subject to income tax.
- *Taxable income* is your earnings which are assessed for income tax. This includes your personal tax allowance but excludes your pension contributions.

3.2 Introduction of a top-rate income tax of 50% from 6 April 2010

Income tax rates for 2009-10 and 2010-11 are set out below.

Income Tax	Taxable Income	
	2009-10	2010-11
Basic rate: 20%	£0-£37,400	£0-£37,400
Higher rate: 40%	Over £37,400	Over £37,400 up to £150,000
Additional rate: 50%	Not applicable	Over £150,000

Definitions:

- *Taxable income* is your earnings which are assessed for income tax. This includes your personal tax allowance but excludes your pension contributions.

3.3 Restriction of higher rate tax relief on pension contributions from 6 April 2011

You will be affected if your gross income is £150,000 per year or over and your pre-tax income is £130,000 per year or over. The level of tax relief will be as follows:

Gross Income per year	Tax relief on pension contributions
Less than £150,000	Highest rate of tax currently paid (40%)
£150,000 to £180,000	On a reducing scale from 50% to 20%
Over £180,000	20%

The detail of the reducing scale on tax relief, between incomes of £150,000 and £180,000 per year, has still to be defined.

This restriction in tax relief will operate by the collection of the excess higher rate tax through an annual tax charge. This will be paid through the yearly self-assessment process at the end of each tax year. Effectively this will claw back the excess higher rate tax relief received. The level of this tax charge is indicated in the table below:

Gross Income per year	Tax Charge (% of pension contributions paid)
Less than £150,000	Not applicable
£150,000 to £180,000	This will be more than 0% but less than 30%. <i>Subject to the detail of the reducing scale of tax relief.</i>
Over £180,000	30%

Example of a possible tax charge

Gross income is a new term and for the purposes of this tax rule makes reference to the increase in your pension benefits, funded by your employer, during the year. As a result gross incomes will be higher than pre-tax incomes.

If your gross income is £185,000 and your pre-tax income is £150,000 per year and you pay £11,250 pension contributions in the 2011/12 year (7.5% contribution rate to the Scheme) your tax charge may be:

$$30\% \times £11,250 = \mathbf{£3,375 \text{ Tax Charge}}$$

Where this tax charge exceeds £15,000 it may be possible to pay this out of your pension fund. Exactly how this would operate is still to be defined.

Definitions:

- *Gross income*, for the purposes of the £150,000 threshold, is your taxable income for the year plus pension contributions you make, plus the value of the growth in your pension benefit funded by your employer. The method for calculating the employer funded growth is not defined yet but will exclude your pension contributions.
- *Pre-tax income* is, in any given year, your total earnings from all sources before the deduction of tax and pension contributions etc.

3.4 An increase of 1% to employee and employer National Insurance Contributions from 6 April 2011

The Chancellor announced an increase of 0.5% to National Insurance Contributions in the 2008 Pre-Budget Report. The further 0.5% increase announced in the 2009 Pre-Budget Report represents a total increase of 1% from 6 April 2011.

3.5 Anti-forestalling rules effective from 22 April 2009

The original anti-forestalling rules were announced in the Chancellor's April 2009 Budget with a threshold of £150,000 relevant income. This threshold was reduced to £130,000 relevant income by the 2009 Pre-Budget Report, effective from midday on 9 December 2009.

If your relevant income is at least £130,000 you may be restricted on the level by which you can increase your pension contributions.

There is also a "look back" test. If your relevant income is below the threshold (£130,000) in the 2009/10 tax year you also need to check whether or not your relevant income was lower than the same threshold for the previous two tax years. If it was not, you are subject to the anti-forestalling rules for the 2009/10 tax year.

The anti-forestalling rules aim to claw back the higher rate tax relief, you would receive, if you increase your pension contributions above the higher of:

- your regular amount; and
- £20,000 (in some cases this can be £30,000) per year before 6 April 2011.

As a result you cannot tax-efficiently increase your pension contributions if you are subject to the anti-forestalling rules.

The tax charge will be 20% in the current tax year and 30% in the next tax year due to the introduction of the 50% rate of income tax from 6 April 2010.

From 6 April 2011 the tax charge and the restriction of higher rate tax relief on pension contributions reverts to the £150,000 threshold as detailed in section 3.3.

Definition:

- *Relevant income* is all earnings and taxable benefits provided by your employer plus any other income including rental income (less allowed losses), share dividends, savings etc less your pension contributions of up to £20,000 less any registered charitable giving.

4. Next Steps

As this is a specialised subject you may wish to consider taking specialist financial or taxation advice. NILGOSC is unable to provide advice on either your taxation or pension arrangements.

This information note is based on our current understanding of the changes. It does not confer any financial or taxation advice and is provided for information purposes only. It should not be a substitute for financial or taxation advice.

The government has published draft legislation and a lengthy consultation document outlining the measures that will take effect from 6 April 2011. Further details on the consultation can be found at:

www.hm-treasury.gov.uk/prebud_pbr09_consult_pensions.htm

I appreciate the complex nature of these changes and I am happy to answer any questions you may have. If you require any further information or clarification please contact either myself, Maddi Frondigoun or Zena Kee by telephone on 0845 3087345 or email me at:

mark.wright@nilgosc.org.uk.

Yours sincerely



Mark Wright
Pensions Development Manager