Lifetime Allowance tax changes from 6 April 2012

Fixed Protection – urgent further guidance

Why are we issuing this further guidance?

Last November we issued a notice for staff 'Tax changes affecting your Civil Service pension' which covered the changes to both the Annual Allowance and the Lifetime Allowance. This further notice provides clarifying guidance on the reduction of the Lifetime Allowance, and in particular the implications of applying for Fixed Protection. This notice should be read in conjunction with the Q and A on pages 5 – 6, and the Lifetime Allowance example on pages 11 -12, of last November's staff notice (available at http://resources.civilservice.gov.uk/wp-content/uploads/2011/11/EPN-310_Annex-A.rtf).

Since we issued the November notice HMRC has provided further guidance and advice on the implications of applying for, and retaining, Fixed Protection. You can access an overview called 'Fixed protection for your pension savings' on HMRC's website at http://www.hmrc.gov.uk/pensionschemes/fixed-protection.htm. This overview contains links to both the application form (APSS227) for fixed protection and HMRC's Pension Schemes Newsletter 50 (Fixed Protection Special Edition) which contains detailed information on applying for fixed protection and the implications of doing so.

In light of this, we are issuing this update to share our understanding of how applying for Fixed Protection might interact with the Rules of the Civil Service pension scheme.

How can I retain fixed protection?

To retain fixed protection in a defined benefit scheme, such as the Civil Service pension scheme, you cannot have any further 'benefit accrual'. The test for fixed protection is a forward looking test that starts immediately after midnight on 6th April (i.e. at 00.01 on 6th April) each year. If you have fixed protection and your pension and any automatic lump sum are increased by an amount which exceeds, in the case of the Civil Service pension scheme, the Consumer Prices Index (CPI) then 'benefit accrual' will have happened and you will lose your fixed protection.

If you remain an active member of the Civil Service pension scheme (with fixed protection) after 5 April 2012 it is possible that the value of your benefits will grow faster than the value of your benefits at 5 April 2012 increased by CPI. As an active member your benefits grow in two ways; the addition of further pension from extra years of reckonable service and an increase to benefits already earned as a result of pay increases (or price indexation in the case of **nuvos**). Circumstances under which you would be more likely to lose fixed protection, due to ‘benefit accrual’, include the following:

1. A pay rise which, together with additional reckonable service, increases the value of your benefits above the value of your benefits at the start of the tax year increased by CPI.

2. The earnings cap in the Civil Service pension scheme is increased each 6 April by the Retail Prices Index (RPI) rounded up to the nearest multiple of £600. In years when this causes the cap to increase by more than CPI, someone subject to the cap (generally, scheme members who joined the Civil Service on or after 1 June 1989) and whose salary is at or above the new tax year’s earnings cap will automatically have ‘benefit accrual’ on 6 April and will lose their fixed protection.

3. Fixed protection will be lost if any contributions are made to money purchase arrangements (such as the Civil Service AVC scheme and stakeholder pension plan).

If you have fixed protection, opting out of the Civil Service pension scheme and stopping building up benefits in every registered pension scheme that you belong to is the only way to guarantee that you have no further ‘benefit accrual’. If you opt out of the Civil Service pension scheme you will become a deferred member and your pension will be preserved and will increase in line with CPI.

What are the implications of a decision to opt out of the Civil Service pension scheme?

Opting out in order to retain fixed protection is not a decision to be taken lightly as you would no longer be covered by the ill-health retirement and death-in-service provisions of the scheme.

The scheme rules currently provide the following death-in-service benefits for active members:

classic and **nuvos:** a death-in-service lump sum of two times pensionable earningsz

premium: a death-in-service lump sum of three times pensionable earnings

If you die after opting out of the Civil Service pension scheme, but before your preserved benefits come into payment, the scheme rules currently provide for payment of the following lump sum death benefits:

classic: a death benefit equal to the preserved lump sum, so effectively three times your preserved pension

premium and **nuvos:** a death benefit of five times your preserved pension

If you opt out of the Civil Service pension scheme, you will not be eligible to receive ill-health retirement benefits under the scheme, although members who opt out of **classic** and fall ill before age 60 may receive immediate payment of their preserved award in certain circumstances.

We strongly recommend that you take independent financial advice if you are considering opting out of the scheme to retain fixed protection.

When would I have to opt out of the scheme?

There is less likelihood of 'benefit accrual' in times of tight pay constraints, although there would still be a risk that future accrual could exceed the CPI limit, at which point fixed protection would be lost.

HMRC has confirmed that an individual applying for fixed protection does not have to make their decision on whether or not to opt out of the scheme by 5 April 2012, although if you are subject to the earnings cap (as set out under 2 above), you should consider taking independent financial advice if you are thinking of delaying your decision to opt out.

Will automatic enrolment have any impact on retaining fixed protection?

You should also be aware that, as part of the Government's Work Place Pensions Reform, from October 2012 onwards large employers will have to automatically re-enrol members, who have previously opted out of their workplace pension scheme, every three years (the requirement on employers is being phased in over a four year period with the largest employers first). If you are re-enrolled in these circumstances you will have to opt out of the scheme again within one month of being auto-enrolled, or (if later) within one month of your employer telling you that you have been auto-enrolled, or you will build up benefits and may lose your fixed protection

Who is responsible for monitoring whether benefit accrual takes place?

HMRC has made it clear that is the member, not the scheme, who is responsible for monitoring their pension position on an ongoing basis. It is therefore your responsibility to notify HMRC if fixed protection no longer applies and you must do so within 90 days of losing fixed protection.

What happens when someone with fixed protection takes their benefits?

If you have fixed protection and you want to rely on it to reduce or eliminate any Lifetime Allowance charges when you take your benefits, then you must tell your scheme administrator that you have fixed protection and provide your fixed protection certificate reference number (and a copy of the certificate, if requested).