OFFICE NOTICE

Do you fill in an income tax return?

Income tax returns for the year to 5 April 2007 cover pensions. Any taxpayer whose pension savings have exceeded the Annual Allowance must report this to HMRC through the self-assessment process.

What is the Annual Allowance?

The Annual Allowance is the total amount you are allowed to put into tax-relieved pension saving in the “input period” ending in a tax year without having to pay any extra tax. For occupational pensions (such as **classic**, **classic plus** and **premium**), the “amount put in” is a notional amount equivalent to 10 times the increase in annual pension plus the increase in any automatic lump sum (this does not apply in **premium**). For the tax year 2006/7 the Annual Allowance is £215,000.

The Cabinet Office, as managers of the Civil Service pension scheme, have set the input period as the period ending 31 December. For the tax year 2006/7 (the first year of the new tax arrangements), the input period is therefore the period from **6 April 2006 to 31 December 2006** (in subsequent years, the input period will be the full year from 1 January to 31 December).

For money purchase pensions, such as AVCs, **partnership** pension account or personal pensions, the “amount put in” is the actual amount you saved. You may be able to set your own input period for money purchase pensions; if the Annual Allowance is an issue for you, you should take independent advice on this point.

Am I affected?

The overwhelming majority of civil servants will be well under the Annual Allowance and have nothing to worry about, as Example 1 below should show. The people typically at risk are:

- high earners who have long service and who have a significant pay rise during the year (see Example 2 below) and/or
- people re-employed at a much higher salary than before, and who aggregate a long period of earlier service (see Example 3 below) and/or
- people making very large contributions to money purchase pensions

The Annual Allowance does not apply to any pension benefits in the year when you have retired and taken your full benefits on retirement. The Annual Allowance also does not apply if you have applied for Enhanced Protection for your pension benefits.

What do I need to do?

If you think that you might be close to or over the Annual Allowance, you must ask your pension administrator (APAC) for an Annual Allowance statement. You will also need to get information from any other pension provider (for instance, if you are paying into a personal pension or AVC).

If you think you are over the Annual Allowance, you may wish to check matters with an independent adviser before submitting your Self Assessment tax return. High earners or their advisers can also email LTA@cabinet-office.x.gsi.gov.uk with questions about the Civil Service pension arrangements.

Examples

Example 1 – Deputy Director

Jane is in **classic**. Jane's pensionable earnings were £64,000 at 31 December 2006 and £56,000 at 6 April 2006. Jane had 30 years' pensionable service on 31 December 2006 and 29.26 years' pensionable service at 6 April 2006.

Jane's **classic** pension at 31 December = £64,000 x 30/80 = £24,000pa plus a lump sum of 3 x pension = £72,000

Jane's **classic** pension at 6 April = £56,000 x 29.26/80 = £20,482pa plus a lump sum of 3 x pension = £61,446.

Increase in Jane's pension = £24,000 - £20,482 = £3,518
Increase in Jane's lump sum = £72,000 - £61,446 = £10,554.

For tax purposes, the increase in Jane's pension benefits
= 10 x £3,518 + £10,554
= **£45,734.**

Jane is nowhere near the Annual Allowance of £215,000

Example 2 (significant promotion)
Ann is promoted to Permanent Secretary on a salary of £160,000. Ann's previous salary as a Director-General was £120,000. Ann has 35 years' service at 31 December (34.25 years at 6 April) and is not subject to the earnings cap. Ann is in **premium**.

Ann's **premium** pension at 31 December = £160,000 x 35/60 = £93,333
Ann's **premium** pension at 6 April = £120,000 x 34.25/60 = £68,500

Increase in Ann's pension = £93,333 - £68,500 = £24,833

For tax purposes, the increase in Ann's pension benefits
= £24,833 x 10 = **£248,330**

Ann has exceeded the Annual Allowance by £33,330 and she must declare this on her tax return, together with any sums paid into a personal pension or AVC. Ann will pay tax at 40% on this amount.

Example 3 (re-employment and aggregation)
George rejoined the Civil Service on 1 July 2006 as Chief Executive of an Agency. He earns £180,000 but, for pension purposes this is restricted to the "earnings cap" of £112,800. On rejoining and going into **premium**, George opted to "aggregate" an earlier period of 29.5 years' service with his current period of service (0.5 years at 31 December 2006). George's preserved pension (from his 29.5 years' service) was £30,000pa.

George's **premium** pension at 31 December = £112,800 x 30/60 = £56,400
George's deferred pension at 6 April = £30,000

Increase in George's pension = £56,400 - £30,000 = £26,400

For tax purposes, the increase in George's pension benefits
= £26,400 x 10 = **£264,000**

George has exceeded the Annual Allowance by £49,000 and he must declare this on his tax return, together with any sums paid into a personal pension or AVC. George will pay tax at 40% on this amount.