NEWCASTLE UNIVERSITY
PENSION TAX AWARENESS BRIEFING

Newcastle University

MAKE TOMORROW, TODAY

MERCER
SECTION 1
SCHEME SPECIFICS
TYPES OF PENSION SCHEMES

THE PENSIONS LANDSCAPE IS CHANGING!

DEFINED BENEFIT (DB)

DEFINED CONTRIBUTION (DC)
TYPES OF PENSION SCHEMES
DEFINED BENEFIT

FINAL SALARY
Benefits based on final pensionable salary at 31 March 2016.
Benefits at 31 March 2016 will then be increased by USS pension increases.

CARE
Benefits based on sum of yearly pensions calculated using the pensionable salary in that year (increased to retirement with inflation)

CARE = Career Average Revalued Earnings
CRB (Career Revalued Benefits) Section in USS
RIB (Retirement Income Builder Benefits) Section in USS

Salaries in early career will not be used to calculate benefits

Yearly pension blocks
TYPES OF PENSION SCHEMES
DEFINED CONTRIBUTION

- Contributions from member and employer invested
- Choice of investment funds
- Default fund has a pre-determined mix of investments
- Freedom to choose what to do with “pot” at retirement

USS Investment Builder Section from 1st October 2016
# Scheme Specifics

## USS

<table>
<thead>
<tr>
<th>Scheme</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Date of change</strong></td>
<td>1 April 2016</td>
</tr>
<tr>
<td><strong>PAST benefits</strong></td>
<td>Linked to inflation</td>
</tr>
<tr>
<td><strong>FUTURE benefits</strong></td>
<td>RIB* up to £55,000, USS IB** from £55,000 (from October 2016)</td>
</tr>
<tr>
<td><strong>Accrual rate</strong></td>
<td>75ths</td>
</tr>
<tr>
<td><strong>Tax free cash</strong></td>
<td>3 times pension</td>
</tr>
<tr>
<td><strong>CARE increases</strong></td>
<td>Limited CPI</td>
</tr>
<tr>
<td><strong>University contributions</strong></td>
<td>18%</td>
</tr>
<tr>
<td><strong>Employee contributions</strong></td>
<td>8%</td>
</tr>
</tbody>
</table>

* Retirement Income Builder  
** Investment Builder
SECTION 2
OVERVIEW OF PENSIONS TAX
OVERVIEW OF PENSIONS TAX
HISTORY OF PENSIONS TAX

PRE 2006
Limits on years of service and contributions

POST 2006
“Tax simplification”!
OVERVIEW OF PENSIONS TAX
TYPES OF PENSIONS TAX

ANNUAL ALLOWANCE (AA)

The maximum value of the benefits built up or total contributions made each year

LIFETIME ALLOWANCE (LTA)

The maximum value of your benefits (pension and cash) on retirement

Exceed an allowance and receive an extra tax charge
SECTION 3
ANNUAL ALLOWANCE
ANNUAL ALLOWANCE
CHANGES SINCE IT WAS INTRODUCED – BEFORE SUMMER BUDGET 2015

<table>
<thead>
<tr>
<th>Year</th>
<th>Annual Allowance</th>
<th>Excess – additional taxation applies</th>
</tr>
</thead>
<tbody>
<tr>
<td>2006</td>
<td>£215,000</td>
<td>£215,000</td>
</tr>
<tr>
<td>2010</td>
<td>£255,000</td>
<td>£255,000</td>
</tr>
<tr>
<td>2011</td>
<td>£50,000</td>
<td>£50,000</td>
</tr>
<tr>
<td>2014</td>
<td>£40,000</td>
<td>£40,000</td>
</tr>
</tbody>
</table>

Have to pay tax on the value above the Annual Allowance

Total HMRC value of annual pension savings
SOME DETAIL ON THE ANNUAL ALLOWANCE

**Defined Benefit**

- **Start of year**
  - Accrued benefit (i.e. benefits worked out on service and salary at start of year)
  - \( \times 16 \) (if cash by commutation)
  - \( \times 19 \) (if cash is 3 times pension)

- **End of year**
  - Accrued benefit (i.e. benefits worked out on service and salary at end of year)
  - \( \times 16 \) (if cash by commutation)
  - \( \times 19 \) (if cash is 3 times pension)

+ CPI

**Defined Contribution**

Amount of contributions paid by member and employer in the year
POSSIBLE MITIGATION

“Carry forward”: Any unused AA in the previous three years can be used in the current year.

“Scheme Pays”: If your AA charge is in excess of £2,000, you can ask your pension provider to pay it from your pension savings.
**Example Before Summer Budget**

*Pat’s salary last year was £80,000, salary this year is £100,000, 25 years of service*

Accrued benefit plus CPI

1 April 2015

£25,300

Accrued benefit £32,500

1 April 2016

(32,500 – 25,300) x 19 = £136,800

**Calculations**

- **Annual Allowance**: £40,000
- **Carry forward from previous 3 years**: £15,000
- **Total allowance**: £55,000
- **Excess above allowance**: £81,800
  (i.e. 136,800 – 55,000)
- **Tax charge**: £32,720
  (assuming 40% marginal tax rate)

If paid via Scheme Pays and assuming a Scheme Pays factor of 20:1 = £1,636 p.a. pension deduction
NEW TAPERED ANNUAL ALLOWANCE

REALIGNMENT OF THE PENSION INPUT PERIOD (PIP)
For people with earnings £150,000 - £210,000 the Annual Allowance will be progressively reduced from £40,000 to £10,000 on a uniform scale from April 2016.
SUMMER BUDGET CHANGES
THE TAPERED ANNUAL ALLOWANCE

Determine **Threshold Income** = Broadly total taxable income (eg salary, bonus, rental income, investment income)

Is **Threshold Income** greater than £110,000?

NO

The member is not subject to the Tapered Annual Allowance. Their Annual Allowance is **£40,000**

NO

Yes

Determine **Adjusted Income** = Threshold Income + any DC contributions + any Pension Input Amount for DB members

Is **Adjusted Income** greater than £150,000

NO

Yes

The member is subject to the Tapered Annual Allowance. Their Tapered Annual Allowance will be between **£10,000** and **£40,000**

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ANNUAL ALLOWANCE FROM 2016/17

WHAT IS “THRESHOLD INCOME”? IT INCLUDES THE FOLLOWING

Basic Salary

Performance related pay

Taxable benefits (e.g. car, medical plan)

Taxable social security benefits

Pensions in payment (including State Pension)

Taxable dividend, rental and savings income

LESS

Your pension contributions

Certain charitable donations

PLUS

Employer contributions to a new salary sacrifice arrangement

WHAT IS “ADJUSTED INCOME”?

THRESHOLD INCOME

PLUS

Pension contributions to a DC arrangement e.g. Investment Builder

Annual pension savings under Retirement Income Builder
Determine Pat’s **Threshold Income**

£100,000 (salary) + £25,000 (e.g. from rental income) = £125,000

Is **Threshold Income** greater than £110,000?

**NO**

The member is not subject to the Tapered Annual Allowance. Their Annual Allowance is £40,000

**NO**

**YES**

Determine **Adjusted Income**

£125,000 (Threshold Income) + £136,800 (Pension Input Amount) = £261,800

Is **Adjusted Income** greater than £150,000?

**NO**

**YES**

Pat is subject to a Tapered Annual Allowance of £10,000
**Summer Budget Changes**

**Realignment of Pension Input Period in 2015/16**

- **£80,000 Annual Allowance in 2015/16**
  - **For one year only!**

**Pre Alignment Tax Year**
- £80,000
  - 1 April 2015 to 8 July 2015
  - 99 days

**Post Alignment Tax Year**
- Max £40,000 carry forward from pre alignment (plus previous carry forward)
  - 9 July 2015 to 5 April 2016
  - 272 days

**Current Pension Input Period started on 1 April 2015**
**EXAMPLE**

**AFTER SUMMER BUDGET – REALIGNMENT PERIOD**

*Pat’s salary last year was £80,000, salary this year is £100,000, 25 years of service*

<table>
<thead>
<tr>
<th>Date</th>
<th>Accrued Benefit</th>
<th>1 April 2015</th>
<th>5 April 2016</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 April 2015</td>
<td>£25,625</td>
<td></td>
<td></td>
</tr>
<tr>
<td>5 April 2016</td>
<td>£32,520</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

\[
(32,520 - 25,625) \times 19 = £131,005
\]

### Calculations

- **Tax charge before summer budget**: £32,720
- **Pre alignment value**: £34,958
  \[
  (131,005 \times 99/(366+5))
  \]
- **Carry forward to post alignment period**: £40,000
  \[
  (80,000 - 34,958 \text{ to a max of £40,000})
  \]
- **Post alignment value**: £96,047
  \[
  (131,005 - 34,958)
  \]
- **Post alignment Annual Allowance**: £40,000
- **Carry forward from previous 3 years**: £15,000
- **Total allowance**: £55,000
- **Excess above allowance**: £41,047
  \[
  (96,047 - 55,000)
  \]
- **Tax charge**: £16,419
  (assuming 40% marginal tax rate)

*If paid via Scheme Pays and assuming a Scheme Pays factor of 20:1 = £821 p.a. pension deduction*
**EXAMPLE FROM APRIL 2017/18**

**Sam’s salary: £100,000.**
**USS provides hybrid benefits.**
**Accrued pension increase in line with CPI:**

Could be worthwhile saving a further £15,000 to maximise tax efficiency

<table>
<thead>
<tr>
<th>Description</th>
<th>Value</th>
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</thead>
<tbody>
<tr>
<td>RIB threshold, £55,000</td>
<td>£55,000</td>
</tr>
<tr>
<td>HMRC value of RIB pension: (£55,000 x (1/75) x 19)</td>
<td>£13,933</td>
</tr>
<tr>
<td>HMRC value of USS Investment Builder: ((12% + 8%) x (£100,000 – £55,000))</td>
<td>£9,000</td>
</tr>
<tr>
<td>HMRC value of the “match” (optional): (2% x £100,000)</td>
<td>£2,000</td>
</tr>
<tr>
<td><strong>Total HMRC value:</strong></td>
<td><strong>£24,933</strong></td>
</tr>
<tr>
<td><strong>Annual Allowance</strong> (adjusted income is less than £150,000)</td>
<td><strong>£40,000</strong></td>
</tr>
<tr>
<td><strong>Carry forward</strong> (i.e. £40,000 - £24,933)</td>
<td><strong>£15,067</strong></td>
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</tbody>
</table>

The HMRC value of the hybrid USS benefits is significantly lower and no AA tax charge is due.
**EXAMPLE FROM APRIL 2017/18**

**BUT:** If Sam’s salary was £150,000.

<table>
<thead>
<tr>
<th>Description</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>RIB threshold</td>
<td>£55,000</td>
</tr>
<tr>
<td>HMRC value of RIB pension:</td>
<td>£13,933</td>
</tr>
<tr>
<td>( (\£55,000 \times \frac{1}{75}) \times 19 )</td>
<td></td>
</tr>
<tr>
<td>HMRC value of USS Investment Builder:</td>
<td>£19,000</td>
</tr>
<tr>
<td>( ((12% + 8%) \times (\£150,000 - \£55,000)) )</td>
<td></td>
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<tr>
<td>HMRC value of the “match” (optional):</td>
<td>£3,000</td>
</tr>
<tr>
<td>( (2% \times \£150,000) )</td>
<td></td>
</tr>
<tr>
<td><strong>Total HMRC value:</strong></td>
<td>£35,933</td>
</tr>
<tr>
<td>Annual Allowance:</td>
<td>£28,784</td>
</tr>
<tr>
<td>(adjusted income is £172,433)</td>
<td></td>
</tr>
<tr>
<td>Assume no carry forward from previous 3 years</td>
<td></td>
</tr>
<tr>
<td><strong>Excess above allowance</strong></td>
<td>£7,149</td>
</tr>
<tr>
<td>(i.e. £35,933 - £28,784)</td>
<td></td>
</tr>
<tr>
<td><strong>Tax charge at 45%</strong></td>
<td>£3,217</td>
</tr>
</tbody>
</table>
WHAT DOES IT MEAN FOR MEMBERS?
RESPONSIBILITIES AND DEADLINES:
EXAMPLE 2015-2016 TAX YEAR

Members to notify HMRC on self assessment tax returns that they want to use Scheme Pays and to have completed self-assessment form.

Latest date for members to make irrevocable election to proceed with Scheme Pays.

HMRC matches up scheme tax payments with elections by members for Scheme Pays on tax returns.

Best practice for Schemes to have sent pension savings statements to those who have exceeded the AA in that scheme.

Date when tax payable from scheme becomes due.

6 Oct 2016
31 Jan 2017
31 July 2017
31 December 2017
February 2018 onwards
### Increase in value of benefits

In tax year after allowing for any available carry forward for the three previous tax years in respect of registered pension scheme.

### Completed if Scheme Pays option exercised

- Enter the amount of Annual Allowance excess tax charge paid or payable by the scheme administrator, who you will have told how much tax has been paid. **Where more than one pension scheme has paid such a tax charge, enter the total.**

### If Scheme Pays is being considered, enter the Pension Scheme tax reference number here

- **Value of pension benefits in excess of your Available Lifetime Allowance, taken by you as a lump sum:** £
- **Value of pension benefits in excess of your Available Lifetime Allowance, not taken as a lump sum:** £
- **Lifetime Allowance tax paid by your pension scheme:** £
- **Amount saved towards your pension, in the period covered by this return, in excess of the Annual Allowance:** £
- **Annual Allowance tax paid or payable by your pension scheme:** £
- **Pension scheme tax reference number:**
- **Amount of unauthorised payment from a pension scheme, not subject to Surcharge:** £
- **Amount of unauthorised payment from a:** £
SECTION 4
LIFETIME ALLOWANCE
CHANGES TO THE LIFETIME ALLOWANCE (LTA)

- **Lifetime Allowance**
- **Excess – additional taxation applies**

2006:
- £1.5m

2010:
- £1.8m

2012:
- £1.5m

2014:
- £1.25m

2016:
- £1.0m (increasing with CPI from 2018)

25% tax free cash - max £250,000 from 2016

25% Lifetime Allowance charge on excess

Total HMRC value of retirement benefits

Pension (taxed)

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SOME DETAIL ON THE LIFETIME ALLOWANCE

HMRC value = Pension x 20 + Cash

EXTRA TAX CHARGE
…if the HMRC value exceeds the Lifetime Allowance
**EXAMPLE LIFETIME ALLOWANCE**

Pat retires with a pension of £75,000, a cash lump sum of £225,000 and a USS Investment Builder pot of £100,000.

Total value = £1,825,000 (i.e. 75,000 x 20 + 225,000 + 100,000)

**Calculations**

Excess over LTA £825,000

(1,825,000 – 1,000,000)

**OPTION:**

- USS pays 25% tax £206,250
- USS Investment Builder pay the first £100,000
- Remaining £106,250 the pension would be reduced by around £5,300 conversion is at 20:1 say

Leaving a pension of £69,700 pa plus cash of £225,000.
CHANGES TO THE LIFETIME ALLOWANCE PROTECTIONS

**Fixed Protection**

- Protects current LTA
- But **you cannot** build up any more benefits in a pension scheme

FP14 is fixed protection at 5 April 2014 (i.e. protected LTA of £1.5m)
FP16 is fixed protection at 5 April 2016 (i.e. protects LTA of £1.25m)

**Individual Protection**

- Protects your **personal** LTA calculated at 5 April to a maximum of current LTA
- Can continue building up benefits in a pension scheme

IP14 is individual protection at 5 April 2014 (i.e. protects LTA of up to £1.5m)
IP16 is individual protection at 5 April 2016 (i.e. protects LTA of up to £1.25m)

Can apply for IP14 up to 5 April 2017
Registration for FP16, IP14 and IP16 will be on line
(No certificates will be issued – only an on line response and a protection reference number)
**Changes to the Lifetime Allowance**

**Individual Protection - Example**

**At 5 April 2016:**
- Pension of £45,000
- Cash of £135,000
- Plus USS Investment Builder “pot” of £100,000

**HMRC Value at 5 April 2016:**
- \[45,000 \times 20 + 135,000 + 100,000 = £1,135,000\]

**Individual Protection**

Don’t pay more tax than HMRC expects you to pay!!
SECTION 5: OPTIONS FOR MEMBERS
OPTIONS FOR MEMBERS OPTING OUT

Affects further build up of benefits

Enhanced opt out

Voluntary Salary Cap

Affects employer contributions
OPTIONS FOR MEMBERS

REMAIN IN THE SCHEME

- Value of past and future benefits (net of income tax)
- Member contributions
- Value of AA and LTA tax
- Net value of benefits

- Value of benefits NOT accrued in future
- Value of AA and LTA tax
- Member contributions
- Net value of benefits

- Reduction in net value

O P T I O N S  F O R  M E M B E R S
COMPARISON OF OPTIONS
STAYING IN USS VS VOLUNTARY SALARY CAP

Cashflow projections: pre-retirement / post-retirement

- Projected take home pay
- Net income in retirement from DC / AVCs
- Projected net DB pension in retirement
- Income tax
- National Insurance Contributions (incl. AVCs)
- Projected Annual Allowance tax charge in year
- Tax Year of Retirement
- Net Income under Status Quo
COMPARISON OF OPTIONS

Net Commercial Value (NCV) at age 65

<table>
<thead>
<tr>
<th></th>
<th>Value £000's</th>
</tr>
</thead>
<tbody>
<tr>
<td>Benefits</td>
<td>1,481</td>
</tr>
<tr>
<td>Pension Tax</td>
<td>1,170</td>
</tr>
<tr>
<td>Benefits</td>
<td>1,123</td>
</tr>
<tr>
<td>Pension Tax</td>
<td>849</td>
</tr>
<tr>
<td>Benefits</td>
<td>1,331</td>
</tr>
<tr>
<td>Pension Tax</td>
<td>1,021</td>
</tr>
<tr>
<td>Benefits</td>
<td>311</td>
</tr>
<tr>
<td>Pension Tax</td>
<td>116</td>
</tr>
</tbody>
</table>

- Benefits: Remain in Scheme
- Benefits: Opt out of Scheme (from October 2016)
- Benefits: Alternative Scenario

NCV of benefits given up to pay LTA tax charges
Tax Free cash
NCV of Income (less EE contributions)
Net Salary Supplement

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SECTION 6: MORE INFORMATION AND NEXT STEPS
### MORE INFORMATION AND NEXT STEPS

<table>
<thead>
<tr>
<th>YOU</th>
<th>ACTION</th>
</tr>
</thead>
<tbody>
<tr>
<td>Be aware of the changes</td>
<td>UNDERSTAND</td>
</tr>
<tr>
<td>Calculate potential impact to you</td>
<td>CALCULATE</td>
</tr>
<tr>
<td>Understand choices and consider your best outcome</td>
<td>CHOOSE</td>
</tr>
<tr>
<td>Implement your decision (e.g. protection application or arranging Scheme Pays for tax bill)</td>
<td>TAKE ACTION</td>
</tr>
<tr>
<td>Review your financial position</td>
<td>REVIEW OFTEN</td>
</tr>
</tbody>
</table>
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