

Press Release

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CHANCELLOR MUST ADOPT A BUDGET FOR PENSIONS

The Government must support good quality pensions by increasing the supply of long-dated and index-linked gilts and abandoning their complex and costly proposals on the tax treatment of pensions contributions. Instead, the Government should adopt the NAPF's alternative approach. This message was delivered¹ this week by the National Association of Pension Funds (NAPF) to the Chancellor of the Exchequer ahead of next month's Budget.

The NAPF has proposed a simpler and fairer approach to pensions taxation which would radically reduce the annual allowance for tax-favoured pension contributions from the current limit of £245,000 to a range of between £45,000 and £60,000. This would work with the grain of existing pensions tax policy and allow government to raise much-needed additional tax revenues. But crucially the NAPF's solution would eliminate some of the arbitrary and unfair consequences of the Government's proposals.

NAPF Chief Executive, Joanne Segars, said:

"The next twelve months will be critical for UK pensions. It is essential that the Government makes the last Budget of this Parliament a Budget for Pensions.

"As recession-hit companies assess the cost and complexity of the pension they offer their employees, the Government must abandon its unworkable pension tax plans that will only serve to damage pension provision in the round.

"Our simpler approach to pensions taxation will avoid the arbitrary and unfair effects of the Government's proposals – too many people outside the Government's target income group are at risk of facing high tax bills just for saving in a pension scheme.

“The Government should also support workplace provision by skewing gilt issuance to the long and index-linked end of the spectrum.”

The impact of the Government’s 2009 tax proposals

The NAPF’s submission:

- Sets out an alternative approach, based on reducing the Annual Allowance. Under the NAPF’s alternative, the Annual Allowance would be reduced from the current £245,000 to a range between £45,000 and £60,000. This would work with the grain of existing pensions tax policy, yet allow the government to raise much-needed additional tax revenues.
- Demonstrates that under the wrong circumstances many people earning salaries between £40,000 and £80,000 a year and not just the top 1% of earners could be caught by the Government’s proposed new regime. This could happen if someone received a promotion, relocation expenses or a redundancy payment (see case studies in annex).
- Shows how, based on research amongst NAPF members, the Government’s proposals are likely to disengage senior company pensions decision makers from pensions. At a time when workplace pensions are in a fragile state, this could further undermine pension provision across the income scale if, ultimately, schemes close.
- Shows how the NAPF’s approach will help companies avoid high and disproportionate implementation costs. Pension experts believe that these are likely to be 10 times higher than the Treasury estimated.
- NAPF analysis suggests that the savings in tax relief to the Treasury under its proposals will be similar to those likely under the Government’s approach. It also finds that the yield from the latter will be between £900 million and £1.5 billion – far lower than the £3 billion estimated.

Increasing the supply of long-dated and index-linked gilts

By increasing the supply of long-dated and index-linked gilts, the Government stands to make a “hat trick of wins”:

- Pension funds would be provided with a strategic asset to match their liabilities and to de-risk at an affordable price.
- UK companies would benefit from reducing the strain of pension scheme volatility on corporate balance sheets.
- The Government will be furnished with a low cost form of finance.

According to the NAPF's recent Annual Survey, pension schemes said increased gilt issuance of this nature would be the single most effective way that the Government could help them to continue provide a defined benefit pension.

ENDS

Notes to Editors

- 1 The NAPF's Budget submission "A Budget for Pensions" will be published on Thursday 25th February on the NAPF website: <http://www.napf.co.uk/policy/recentreports.cfm>

About the National Association of Pension Funds

The NAPF is the leading voice of workplace pensions in the UK. We speak for 1,200 pension schemes with some 15 million members and assets of around £800 billion. NAPF members also include over 400 businesses providing essential services to the pensions sector.

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Annex

Case studies - How those earning far less than £130,000 a year can be affected

A) Janet – the mid-career high achiever on £70,000 a year

Janet is a Chief Accountant aged 45 on a basic salary of £70,000 and is eligible for a performance bonus of £35,000 a year. She receives a car allowance of £8,000 per year and other benefits worth £2,000 a year. Janet has been with the company and in the DB pension scheme (1/60th accrual) for 20 years.

Janet is promoted to Financial Controller receiving a salary increase of £10,000 per year. It has been a very successful year for her employer and Janet has met her objectives so she also receives her maximum bonus of 50% of base salary. Her total income is now £130,000.

Janet's income is now higher than the income 'floor' (£130,000) and so the deemed

value of her employer contributions must be calculated and then added to her current income, to establish her gross income. As Janet is in a good DB scheme the deemed contributions are calculated as being £54,000, bringing her gross income for the purpose of the new pensions tax regime to £184,000. Janet will now become subject to a tax recovery charge of £14,200 – a figure greater than her £10,000 per year salary increase.

B) Dave – the successful manager on £40,000 a year who has to relocate with his job

Dave is a Sales Manager aged 50. He is on a salary of £40,000 a year and is eligible for a performance bonus of £12,000. He also receives a car allowance of £5,000. He has been with the company for 25 years and has been in the (1/50th) DB pension scheme for 25 years.

Dave receives a promotion to Area Sales Manager with a salary increase of £10,000 per year and a larger potential bonus of £15,000 a year. However, to get this new role, he has to move to another part of the country. The company provides him with a relocation package of £40,000 which, when grossed up for tax purposes, amounts to £67,000. As a result, his total income is now £137,000.

Dave's income is now higher than the income 'floor' (£130,000) and so the deemed value of his employer pension contributions must be calculated and then added to his current income. Although originally only on a basic salary of £50,000 a year, due to the relocation package his gross income is now calculated as £137,000.

As the employer's deemed DB contributions are calculated as being the equivalent of £120,000, for the purposes of the new tax regime, Dave's gross income will be calculated as £257,000 and he will be required to pay a tax recovery charge of £34,700, which is more than three times greater than his salary increase.

c) John – the middle ranking executive who gets made redundant due to the recession

John is an HR Manager aged 59. He is on a salary of £80,000 a year. He also receives a car allowance of £5,000. He has been with the company and a member of the (1/60th) DB pension scheme for 20 years

John is made redundant and receives a redundancy payment of 1 x salary (£80,000) of which the initial £30,000 is tax exempt. John's income is now higher than the income 'floor' (£130,000) and so the deemed value of his employer contributions must be calculated and then added to his calculated income of £135,000 to establish his gross income. As John is in a good DB scheme the deemed contributions are calculated on a prescribed formula, which in John's case includes allowance for payment of an unreduced pension from age 60, as £137,400. This brings his gross income for the purpose of the new pensions tax regime to £272,400. John will now become subject to a tax recovery charge of £39,720 plus £20,000 tax on the net redundancy payment - a total tax charge of £59,720.