Pensions Tax Relief
Room 2/E2, HM Treasury
1 Horse Guards Road,
London,
SW1A 2HQ

Our Ref: PS/PM

Your Ref:

Direct Line: 0151 242 1390

Please ask for: Peter Mawdsley

Date: 26 August 2010

Dear Sirs,

RESTRICTION OF PENSIONS TAX RELIEF: CONSULTATION ON ALTERNATIVE APPROACH

I refer to the above mentioned discussion document dated July 2010 and am responding to the invitation for comments on behalf of Wirral Council in its capacity as the Administering Authority of the Merseyside Pension Fund.

Wirral Council is responsible for the administration of the Merseyside Pension Fund which is part of the Local Government Pension Scheme (LGPS). The Merseyside Pension Fund deals with the LGPS pension administration and investments on behalf of the 5 Merseyside District Councils, and over 100 other employers on Merseyside and elsewhere throughout the UK.

The Fund has over 50,000 active contributing members, 41,359 pensioners and just over 34,000 deferred pensioners. It is responsible for the investment and accounting for a pension fund of £4.5 billion. The LGPS is a defined benefit, final salary public sector occupational scheme.

Whilst the Fund welcomes the Government's acceptance that the measures currently due to come into force next April to limit tax relief on pensions contributions have serious technical flaws and will result in unacceptable and inequitable tax charges for some high earners, it is nevertheless concerned that any alternative system does not introduce other equally undesirable consequences and difficulties, for much larger numbers of members of defined benefit schemes, their employers and those running the Funds.

After a prolonged period of discussion with experts within the pensions industry the previous Administration introduced the current simplified tax regime for pensions from 6 April 2006 (A day), including the concepts of the Annual and the Lifetime Allowance which were set at what was agreed to be maximum reasonable levels for an individual to make pension provision with tax relief over a working life.

One of the stated aims of successive Government's has been to encourage people to save towards adequate financial provision for their retirements with the benefit of the incentive of tax relief on pension contributions in the knowledge that this would reduce the amount of means tested State welfare benefits payable in the long term.

The Fund is concerned that the potential for increased complexity, confusion, compliance costs, and perceived unfairness in the latest proposals for changes to the system of calculating tax relief will only further undermine support for pensions savings from employees and employers as a whole, leading to less pensions saving and as a result increased future costs in terms of State welfare provision.

The Fund is therefore particularly concerned that any new system of tax relief takes account of the characteristics of defined benefit schemes like the LGPS and would ask you to properly consider whether using age related factors to convert defined benefit accrual into an equivalent "contribution" which would treat all employees fairly may be better than the use of flat rate factors.

The Fund would support the view that the Annual Allowance charge should be calculated on current accrual only and should not be applied retrospectively.

The Fund's actuary has suggested that under the latest proposals employees on incomes just above the higher rate tax threshold could inadvertently become liable for tax charges greater than the amount of pension they have accrued. The proposals would also appear to risk encouraging the current generation of senior management to drop out of pension provision, undermining enthusiasm for the whole pensions saving regime.

In its submission dated 23 August 2010 the Head of Pensions of the Local Government Employers Organisation (LGE) has illustrated a number of significant difficulties with the impact that the latest proposals would have on large numbers of members of defined benefits schemes such as the LGPS and the administrators of these schemes, these include:

- The fact that the statement made that "the approach of restricting tax relief through existing allowances would affect the highest pension savers" is not true in relation to members of defined Benefit Schemes as a result of the method of valuing benefit accrual in such schemes as the LGPS.

- Concerns about the ability of the new proposals to ensure fairness of treatment between members of defined benefit and defined contribution schemes a problem which the Fund does not believe has been resolved.

- Problems of potential indirect age discrimination in a defined benefit scheme because older employees are more likely to have longer periods of pensionable membership they are more likely to suffer a tax charge than younger employees as illustrated in the examples set out in the LGE response.

- Problems of potential indirect sex discrimination in a defined benefit scheme because significantly more women than men work part time, therefore proportionately more men than women are likely to become subject to a tax charge (See example in LGE response).

The Fund does not support the change proposed to apply the revised annual check in the year of retirement and in particular believes that all ill health retirements should continue to be exempt from such checks.

Alternative Approaches for consideration to delivering savings

If the Government believes that reductions in the value of tax relief which are currently allowed under the existing system are necessary the Fund would suggest that consideration be given to reintroduction of a mandatory maximum pensions earnings cap for future benefits accrual.
Prior to 6 April 2006 there was a maximum permitted pay to be used for calculation of tax approved pension benefits and on which contributions and tax relief could be calculated (Section 590C of the Income and Corporation Taxes Act 1988). If such an earnings cap was reintroduced, coupled with a maximum contribution limit (calculated as a specified percentage of the earnings cap figure) the required cost savings could be delivered much more simply and cheaply in terms of administration. Restricting the pay eligible for tax relief in the first instance would eliminate the need for complex annual calculations, monitoring and compliance and individuals being faced with unexpected tax charges after the event.

Alternatively it could be argued that another simpler and more equitable way of delivering the policy objective of cost savings would be to limit tax relief on employee contributions to basic rate (20%) for all employees either on all pay or on an annual maximum amount related to the current or revised annual and lifetime allowances.

With the planned timescales for change being April 2011 as set out in the discussion document, the timescales for consultation or even communication of the outcomes with scheme employers and members and changes to computer systems and literature would appear virtually impossible.

If you require any further information or assistance please do not hesitate to contact me.

Yours sincerely

Deputy Head of Pension Fund