Family pension plans

Who is likely to be affected?

Employees who, as part of their flexible remuneration package, have pension contributions made by their employer paid into family members' registered pension schemes.

Employers who offer family pension plans as part of their flexible remuneration package to employees.

General description of the measure

This measure will ensure that where an employer pays a pension contribution to a registered pension scheme of an employee's spouse or family member as part of the employee's flexible remuneration package, the value of the contribution will give rise to tax and National Insurance contribution (NIC) liabilities on the employee and the employer respectively.

Policy objective

The measure aligns with the Government's objective of a system of pensions tax relief that is fair, affordable and sustainable. Reform of the pensions tax regime is also an integral part of the Government's deficit reduction plans and the Government will clamp down on action that runs contrary to the policy objective of this reform.

Background to the measure

The Government announced at Budget 2012 that it will take action to prevent an existing exemption from being exploited in a way which was not envisaged when the legislation was introduced.

Detailed proposal

Operative date

The measure will have effect on and after 6 April 2013.

Current law

The current pensions tax rules for registered pension schemes came into force on 6 April 2006 (A-day) and are set out in Part 4 of the Finance Act (FA 2004).

An individual receives tax relief at their marginal income tax rate on their pension savings (section 188 FA 2004). Although there are no limits to how much can be saved in registered pension schemes, there is an overall limit on the total amount of an individual's tax-relieved annual pension savings, including employer contributions, known as the annual allowance (sections 228 to 238 FA 2004). The annual allowance is £50,000 for the tax year 2012-13.

In addition to tax relief on individual contributions, section 308 Income Tax (Earnings and Pensions) Act 2003 (ITEPA) provides that no liability to income tax arises in respect of earnings where an employee's employer makes contributions under a registered pension scheme.

Employers' contributions paid into employees' registered pension schemes are deductible as an expense for corporation tax purposes so long as they meet the requirements of the wholly and exclusively test for the purposes of the employer's trade as detailed in section 74(1)(a) Income and Corporation Taxes Act 1988 and section 34 Income Tax (Trading and Other Income) Act 2005. Such contributions are also disregarded in the calculation of earnings in respect of all contributions paid by an employer to which section 308 of ITEPA applies. Therefore such contributions do not attract employers' NICs (SI 2001/1004 Schedule 3).

Proposed revisions

Legislation will be introduced in Finance Bill 2013 to amend Section 308 ITEPA to restrict the employee's income tax exemption to employer contributions made to the employee's registered pension scheme, rather than contributions made to any registered pension scheme.

Summary of impacts

<table>
<tr><td rowspan="3">Exchequer impact (£m)</td><td>2012-13</td><td>2013-14</td><td>2014-15</td><td>2015-16</td><td>2016-17</td><td>2017-18</td></tr>
<tr><td>-</td><td>negligible</td><td>negligible</td><td>negligible</td><td>negligible</td><td>negligible</td></tr>
<tr><td colspan="6">This measure is expected to have a negligible impact on the Exchequer. Any impact will be set out at Budget 2013. This measure supports the Exchequer in its commitment to protect revenue.</td></tr>
<tr><td>Economic impact</td><td colspan="6">This measure is not expected to have significant economic impacts.</td></tr>
<tr><td>Impact on individuals and households</td><td colspan="6">The number of individuals and households impacted by this measure is expected to be very small and the impact on those who choose to partake in such arrangements, where their employer offers them, to be limited. The measure will put the individuals back in the position the legislation intended with tax efficient employer support for pension savings limited to their employees’ pensions only.</td></tr>
<tr><td>Equalities impacts</td><td colspan="6">This measure does not impact any protected equality group.</td></tr>
<tr><td>Impact on business including civil society organisations</td><td colspan="6">The impact of this measure is considered to be negligible for all businesses. Businesses who offer such arrangements as part of flexible remuneration packages will still be able to do so, but the tax incentives for the employee will be removed as the payment will be taxed as a benefit in kind and the employer would be subject to employer NICs on such payments. Businesses will have to report such payments in line with other employee benefits through the normal payroll processes.</td></tr>
<tr><td>Operational impact (£m) (HMRC or other)</td><td colspan="6">The additional costs for HM Revenue & Customs in implementing this change are anticipated to be negligible.</td></tr>
<tr><td>Other impacts</td><td colspan="6"><u>Small firms impact test</u>: the impact on small firms has been considered but as the measure is about exploitation of the legislation in a way it was not envisaged it would not be appropriate to exclude small firms from the measure. However, the impact of these changes on all businesses is considered to be negligible.

Other impacts have been considered and none have been identified.</td></tr>
</table>

Monitoring and evaluation

The measure will be kept under review through communication with affected taxpayer groups.

Further advice

If you have any questions about this change, please contact Jon Prothero on 020 7147 2785 (email: pensions.policy@hmrc.gsi.gov.uk).

1 Exemption from income tax of contributions to pension schemes

(1) In Chapter 9 of Part 4 of ITEPA 2003 (exemptions from income tax for pension provision), in section 308 (exemption of contributions to registered pension scheme), at the end insert "in respect of the employee".

(2) The amendment made by this section has effect for the tax year 2013-14 and subsequent tax years.

EXPLANATORY NOTE

EXEMPTION FROM INCOME TAX OF CONTRIBUTIONS TO PENSION SCHEMES

SUMMARY

1. This clause restricts an employee's exemption from income tax on pension contributions made by their employer to a registered pension scheme. The restriction ensures that the exemption will only apply to such contributions made by an employer to their employee's arrangements under a registered pension scheme.

DETAILS OF THE CLAUSE

2. Section 1 of the clause inserts the words "in respect of the employee" at the end of Section 308 of Income Tax (Earnings and Pensions) Act 2003 ("ITEPA"). This means that an employee's exemption from income tax on an employer's contribution to a registered pension scheme will not apply where the contribution is made in respect of someone other than the employee.

3. Section 2 provides that the restriction has effect for the tax year 2013/14 and for subsequent tax years.

BACKGROUND NOTE

4. Employees are exempt from income tax on contributions paid into registered pension schemes by their employers. This income tax exemption is provided by Section 308 ITEPA 2003.

5. Where employer pension contributions are exempt from income tax in this way, they are also excluded from earnings for the purposes of earnings-related National Insurance contributions (NICs).

6. The amount of pension contributions that benefit from tax relief is limited to an annual allowance. This allowance was reduced from £255,000 to £50,000 from the tax year 2011-12 and to £40,000 for the tax year 2014-15 onwards.

7. In response to the introduction of the lower limit in 2011-12, certain arrangements (referred to as Family Pension Plans) have been developed to side step the new rules for employees who would

otherwise face an income tax charge on contributions in excess of the £50,000 limit.

8. Under these arrangements, an employer pays pension contributions into a registered pension scheme of an employee’s family member as part of the employee's flexible remuneration package. The effect is that the employee is still exempt from income tax and NICs on the employer contributions into the family member’s pension scheme. Furthermore, these contributions do not count towards the £50,000 limit for the employee, avoiding the income tax that would otherwise be due on the employee for contributions in excess of the limit.

9. This clause ensures that employees will not enjoy exemption from income tax and NICs on such contributions into the family member’s pension scheme, to protect against attempts to sidestep the Annual Allowance limit.

10. If you have any questions about this change, or comments on the legislation, please contact Jon Prothero on 020 7147 2785 (email: jon.prothero@hmrc.gsi.gov.uk).