

# **Employer Asset-backed Pension Contributions**

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## **Who is likely to be affected?**

Sponsoring employers, scheme administrators and trustees of registered pension schemes that are using or considering using asset-backed pension contribution arrangements ('ABC arrangements').

Advisors for these employers, pension scheme administrators and trustees.

## **General description of the measure**

Legislation has been introduced under Finance Bill 2012 to ensure that the amount of tax relief given to employers using ABC arrangements reflects accurately the total amount of payments the employer makes to the pension scheme directly or through a special purpose vehicle (for example a partnership).

## **Policy objective**

The main purpose of this measure is to remove any unintended and excessive tax relief being given to an employer in respect of any asset-backed contributions (ABCs) made to their pension schemes. The Government is also keen to retain as much flexibility as possible for employers to continue to be able to use ABC arrangements to manage their pension deficits, provided any tax risk to the Exchequer is prevented.

This measure is consistent with other measures the Government has already undertaken to ensure that pensions tax relief remains fair and sustainable in the long term. It maintains the principle that pension tax relief is provided for the actual value of contributions made by an employer to their pension scheme, but that tax relief beyond the value of such contributions at a cost to the Exchequer should not be allowed.

## **Background to the measure**

The Government announced in Budget 2011 that it would consult on changing tax rules to remove unintended and excess relief on ABCs.

The consultation document 'Employer Asset-backed Pension Contributions' was published on 24 May 2011 and the consultation closed on 16 August 2011.

## **Detailed proposal**

### **Operative date**

This measure will have effect on and after 29 November 2011.

### **Current law**

All statutory references in this note relate to Finance Act (FA) 2004 unless otherwise specified.

The legislation covering pensions tax relief is in Part 4 of FA 2004. Tax relief on employer contributions to a registered pension scheme (under sections 196 to 200) is given by allowing contributions to be deducted as an expense in computing the profits of a trade,

profession or investment business so reducing the amount of an employer's taxable profit. Tax relief is only given for contributions that have actually been paid. Any contributions must be monetary contributions although it is possible for an employer to enter into an offset arrangement so that the debt for the contribution is offset against a debt to purchase an asset from the employer. In such arrangements, the contribution is paid on the date when the employer and pension offset the two debts.

Certain funding arrangements are structured in such a way that the employer receives a deduction for the contribution paid to a pension scheme upfront, but the pension scheme only receives the cash payments over the term of the arrangement. Where the arrangement involves an asset and this asset generates an income stream to the pension scheme, it is possible for the employer to obtain both a deduction for the pension contribution upfront and then receive another deduction for income payments derived from the asset. In other words, unintended and excessive tax relief can arise under such circumstances.

Some asset-backed arrangements provide for a final payment ('final bullet payment') that is made at the end of the arrangement period but only if the pension deficit remains at that time. Under the current legislation, if the final bullet payment is not actually made, or if the value of the final bullet payment is less than the amount of tax relief received upfront, this could mean that the employer will have obtained excess relief at the start of the arrangement.

The structured finance regime is set out for corporation tax purposes in Chapter 2 of Part 16 of Corporation Tax Act 2010 with mirroring provisions for income tax in Chapter 5B of Part 13 of Income Tax Act 2007. It applies where a person enters into a "structured finance arrangement". A structured finance arrangement (or "SFA") is an arrangement where in accordance with the Generally Accepted Accounting Practice<sup>1</sup>, a person ("the borrower") records in its account a financial liability in respect of the lump sum advance paid by "the lender". In the context of ABCs, where the funding arrangement falls within the SFA rules, excessive tax relief does not arise.

## **Proposed revisions**

Legislation will be introduced in Finance Bill 2012 to make changes to FA 2004 as follows:

Where an ABC arrangement is set up with the employer contribution paid on or after 29 November 2011:

- If the arrangement is accounted for in the accounts of the employer or the special purpose vehicle (if used) as a financial liability such that the SFA rules will apply, then tax relief in the form of an upfront tax deduction will be given for the contribution under the ABC arrangement in the period of account that it is paid. Relief will also be available for the element of subsequent income payments, (if any), that is accounted for as a finance charge in relation to the financial liability recorded in the accounts. In other words, further tax relief on the remaining income payments, excluding any payment of interest charges, will not arise due to the operation of the SFA rules.
- If the arrangement does not fall within the SFA rules, upfront tax relief will not be available. Relief will only be available for subsequent income payments made to the pension scheme under the arrangement. If an income stream providing the

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<sup>1</sup> This is defined under section 1127 Corporation Tax Act 2010 to include both the UK Generally Accepted Accounting Practice and International Financial Reporting Standard.

employer with income payments has been transferred to the pension scheme under the arrangement, these income amounts are likely to cease to be chargeable.

- Where the accounting treatment of an ABC arrangement was initially accounted for as a financial liability (as set out in the first bullet above) and has gained upfront relief, but subsequently changes so that the liability is no longer shown in the accounts or is otherwise reduced by an event other than the making of payments by the employer, then a balancing tax charge will arise to recover tax relief from the employer. This will be achieved by treating the outstanding amount of the financial liability immediately before it is no longer recognised or reduced in the accounts, as a profit or income arising on a loan relationship.
- An anti-avoidance rule will provide that where after the employer has entered into the ABC arrangement that falls within the SFA rules, the employer becomes a party to an avoidance arrangement where the main or one of the main purposes is to enable the total amount of relief given in respect of the employer's contribution to exceed the total amount of the payments passed to the pension scheme under the ABC arrangement, any excess of the upfront tax relief given will be recovered from the employer. Where the avoidance arrangement is entered into at the same time as the ABC arrangement or earlier, the upfront relief will be denied.

Where an ABC arrangement has been set up with the employer contribution paid before 29 November 2011:

- If the ABC arrangement falls within the SFA rules, the tax treatment will remain unchanged at the commencement of the new legislation. However, if the financial liability recorded for the arrangement is reduced by an event other than the making of payments by the employer and the event takes place on or after 29 November 2011, the recovery provision set out in the penultimate bullet above will also apply.
- If the ABC arrangement would not have qualified for upfront relief under the new legislation if it was carried out now, deductions will not be available in relation to the income payments derived from the asset that are made on or after 29 November 2011. Also from the same date, any income amounts that would have been charged to tax if not for the ABC arrangement will be brought back into tax as a charge on the employer or a person connected with the employer or other relevant person as appropriate.
- Where such an arrangement comes to an end, an adjustment will be made so that if the upfront relief allowed exceeds the actual value received by the pension scheme during the arrangement, then any excess of the upfront tax relief will be recovered. This adjustment will take into account the payments made to the pension scheme and the deductions given to the employer before and after 29 November 2011. It will also take into account any payments that could be a finance charge if the arrangement were a SFA and return any relief that would have been denied at or before the end of the arrangement on these "deemed" finance charges under the rule set out immediately above. Where the upfront relief is less than the value received, the employer will be given additional relief for the excess of the value given to the pension scheme.
- When there is a change to the original arrangement period, then the original ABC arrangement will be treated as ended for tax purposes and any excess of the upfront tax relief will be recovered from the employer.

## Summary of impacts

<b>Exchequer impact (£m)</b>	2011-12	2012-13	2013-14	2014-15	2015-16	2016-17
	+£340	+£450	+ £450	+ £450	+ £450	+ £450
	These figures are set out in Table 2.1 of the Autumn Statement and have been certified by the Office of Budget Responsibility. More detail can be found in the policy costings document published alongside the Autumn Statement.					
<b>Economic impact</b>	The Government expects the economic impact to be limited as full tax relief will continue to be available to the employer on the value received by the pension scheme.					
<b>Impact on individuals and households</b>	This measure will have no impact on individuals and households as the changes relate only to the amount of tax relief employers should receive in respect of their asset-backed pension contributions.					
<b>Equalities impacts</b>	The measure only applies to businesses and their associated pension schemes and therefore it is not expected that the policy would impact on any equality groups or people with protected characteristics adversely or disproportionately.					
<b>Impact on business including civil society organisations</b>	The Government expects about a dozen large employers (including those in the civil society organisations) with associated (predominantly defined benefit) pension schemes would be affected by this measure each year. No new obligations have been placed on business as a result of the changes and when tax relief is given will be dependent on the normal accounting process. However, employers or pension schemes which may be affected may need to make some changes to their existing internal processes to ensure that any recovery of excessive relief arising from changes to their ABC arrangements can be made. The administrative cost is expected to be negligible.					
<b>Operational impact (£m) (HMRC or other)</b>	This measure will have no impact on HMRC's operating costs as the normal accounting and compliance processes would be followed.					
<b>Other impacts</b>	<p>Small Firms Impact Test: No responses were received from small firms, however the impact on small firms has been considered. It would not be appropriate for the policy to apply differently according to the size of firms although the measure is unlikely to impact any small businesses since, these arrangements have to date only been used by very large companies with defined benefit pension schemes due to the complexity and transaction costs involved.</p> <p>Impacts of the policy on the following have also been considered: competition, carbon, justice, sustainable development, the wider environment, health, rural proofing, and privacy. It is believed that the policy does not impact unduly on any of these areas.</p>					

**Monitoring and evaluation**

The measure will be monitored through information collected from tax returns, receipts and other statistics.

**Further advice**

If you have any questions about this change, please contact Windy Kwok on 0207 147 2835 or Paul Cottis on 0115 974 2420 (email: [pensions.policy@hmrc.gsi.gov.uk](mailto:pensions.policy@hmrc.gsi.gov.uk)).

**Declaration**

Mark Hoban MP, Financial Secretary to the Treasury has read this Tax Information and Impact Note and is satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impacts of the measure.

**1 Employer asset-backed pension contributions**

Schedule 1 contains provision about contributions paid by employers under registered pension schemes.

## SCHEDULES

### SCHEDULE 1

Section 1

#### EMPLOYER ASSET-BACKED PENSION CONTRIBUTIONS

#### PART 1

#### MAIN PROVISION

- 1 In Chapter 4 of Part 4 of FA 2004 (registered pension schemes: tax reliefs and exemptions) after section 196A insert –

**“196B Employer asset-backed contributions: denial of relief (1)**

- (1) An employer (“E”) is not to be given relief in respect of a contribution (“E’s contribution”) paid by E under a registered pension scheme if conditions A, B and C are met.
- (2) Condition A is that –
  - (a) under an arrangement (“the asset-backed arrangement”) –
    - (i) a person (“the borrower”) receives money or another asset (“the advance”) from another person (“the lender”),
    - (ii) the borrower, or a person connected with the borrower, makes a disposal of an asset (“the security”) to or for the benefit of the lender or a person connected with the lender, and
    - (iii) the lender, or a person connected with the lender, is entitled to payments in respect of the security,
  - (b) the borrower is E or a person connected with E, and
  - (c) the advance is (wholly or partly) paid or provided by the lender out of E’s contribution (directly or indirectly),and the case is not one in relation to which either condition A in section 196C or condition A in section 196D is met.
- (3) For the purposes of subsection (2)(a)(iii) it does not matter if an entitlement of the lender, or a person connected with the lender, is subject to any condition.
- (4) Condition B is that the asset-backed arrangement is not a structured finance arrangement.
- (5) Condition C is that it is reasonable to suppose that the amount of one or more of the payments mentioned in subsection (2)(a)(iii) has been, or is to be, determined (wholly or partly) on the basis that, in essence, the whole or a part of the advance represents a loan which is (wholly or partly) to be repaid by way of one or more of those payments.

- (6) For the purposes of subsection (5) it does not matter that—
  - (a) the repayment of the loan might be subject to any condition, or
  - (b) that the accounts of any person do not record a financial liability in respect of the whole or a part of the advance or that the whole or a part of the advance is not otherwise treated as representing a loan for the purposes of the accounts of any person,

but, subject to that, all relevant circumstances are to be taken into account in order to get to the essence of the matter.

- (7) For the purposes of this section—
  - (a) the borrower and the lender are not connected with one another if that would otherwise be the case,
  - (b) if the borrower is not E, references to a person connected with the borrower include a person connected with E who would not otherwise be connected with the borrower, and
  - (c) “loan” includes any advance of money.

#### **196C Employer asset-backed contributions: denial of relief (2)**

- (1) An employer (“E”) is not to be given relief in respect of a contribution (“E’s contribution”) paid by E under a registered pension scheme if conditions A and B are met.
- (2) Condition A is that—
  - (a) under an arrangement (“the asset-backed arrangement”) a person (“the transferor”) makes a disposal of an asset (“the security”) to a partnership,
  - (b) the transferor is E or a person connected with E,
  - (c) the transferor, or a person connected with the transferor, is a member of the partnership immediately after the disposal (whether or not a member immediately before it),
  - (d) under the asset-backed arrangement the partnership receives money or another asset (“the advance”) from a person (“the lender”) other than the transferor,
  - (e) the advance is (wholly or partly) paid or provided by the lender out of E’s contribution (directly or indirectly),
  - (f) there is a relevant change in relation to the partnership (see section 196E), and
  - (g) under the asset-backed arrangement the share in the partnership’s profits of the person involved in the relevant change (see section 196E) is determined by reference (wholly or partly) to payments in respect of the security.
- (3) If the transferor is not E, for the purposes of this section references to a person connected with the transferor include a person connected with E who would not otherwise be connected with the transferor.
- (4) For the purposes of subsection (2)(g) it does not matter if any determination of the share in the partnership’s profits of the person involved in the relevant change as mentioned is subject to any condition.



- (5) Condition B is that the asset-backed arrangement is not a structured finance arrangement.

**196D Employer asset-backed contributions: denial of relief (3)**

- (1) An employer (“E”) is not to be given relief in respect of a contribution (“E’s contribution”) paid by E under a registered pension scheme if conditions A and B are met.
- (2) Condition A is that—
- (a) a partnership holds an asset (“the security”) at any time before an arrangement (“the asset-backed arrangement”) is made,
  - (b) under the asset-backed arrangement the partnership receives money or another asset (“the advance”) from another person (“the lender”),
  - (c) the advance is (wholly or partly) paid or provided by the lender out of E’s contribution (directly or indirectly),
  - (d) there is a relevant change in relation to the partnership (see section 196E), and
  - (e) under the asset-backed arrangement the share in the partnership’s profits of the person involved in the relevant change (see section 196E) is determined by reference (wholly or partly) to payments in respect of the security.
- (3) For the purposes of subsection (2)(e) it does not matter if any determination of the share in the partnership’s profits of the person involved in the relevant change as mentioned is subject to any condition.
- (4) Condition B is that the asset-backed arrangement is not a structured finance arrangement.

**196E What is a “relevant change in relation to the partnership” etc?**

- (1) For the purposes of sections 196C and 196D there is a relevant change in relation to the partnership if condition X or Y is met.
- (2) Condition X is that, in connection with the asset-backed arrangement, the lender or a person connected with the lender becomes a member of the partnership at any time.
- (3) Condition Y is that—
- (a) in connection with the asset-backed arrangement, there is at any time a change in a member’s share in the partnership’s profits, and
  - (b) the member is the lender or a person connected with the lender or a person who in connection with the asset-backed arrangement becomes at any time connected with the lender.
- (4) For the purposes of subsections (2) and (3) an event occurs in connection with the asset-backed arrangement if it occurs directly or indirectly in consequence of it or otherwise in connection with it.
- (5) For the purposes of sections 196C and 196D references to the person involved in the relevant change are—

- (a) if it is condition X that is met, to the lender or the person connected with the lender (as the case may be), and
- (b) if it is condition Y that is met, to the member of the partnership in whose share in the partnership's profits there is a change.

#### **196F Employer asset-backed contributions: anti-avoidance**

- (1) This section applies if—
  - (a) an employer (“E”) pays a contribution (“E’s contribution”) under a registered pension scheme,
  - (b) conditions A and C in section 196B are met or condition A in section 196C or 196D is met,
  - (c) the asset-backed arrangement is a structured finance arrangement and, accordingly, condition B in section 196B, 196C or 196D (as the case may be) is not met,
  - (d) at any time (“the relevant time”) E, or a person connected with E, enters into an arrangement (“the avoidance arrangement”), and
  - (e) the main purpose, or one of the main purposes, of E or the person connected with E in entering into the avoidance arrangement is to secure that the total amount of the relevant payments will be less than the amount of E’s contribution.
- (2) If the relevant time is the same as the time at which the advance is received or earlier, section 196B, 196C or 196D (as the case may be) applies in relation to E’s contribution as if condition B in that section were met.
- (3) Otherwise, the amount of the relevant financial liability as at the relevant time is treated as follows—
  - (a) if E is within the charge to corporation tax at the relevant time, the amount is treated as if it were a profit which E has in respect of E’s loan relationships chargeable to corporation tax under section 299 of CTA 2009 for E’s accounting period in which the relevant time falls, or
  - (b) otherwise, the amount is treated as if it were an amount of income of E chargeable to income tax under Chapter 8 of Part 5 of ITTOIA 2005 for the tax year in which the relevant time falls.
- (4) The amount treated as profit or income by subsection (3)(a) or (b) is not to exceed the total amount of relief given in respect of E’s contribution.
- (5) For the purposes of this section—
  - (a) “the advance” and “the asset-backed arrangement” have the same meaning as in section 196B, 196C or 196D (as the case may be),
  - (b) “the relevant financial liability” means the financial liability mentioned in section 809BZA(3), 809BZF(3) or 809BZJ(3) of ITA 2007 or section 758(3), 763(3) or 767(3) of CTA 2010 (as the case may be) in respect of the advance,
  - (c) “the relevant payments” means the payments which reduce that liability as so mentioned, and

- (d) the amount of the relevant financial liability as at the relevant time is to be determined in accordance with generally accepted accounting practice.

**196G Employer asset-backed contributions: reduction of financial liability under structured finance arrangement**

- (1) This section applies if –
- (a) an employer (“E”) pays a contribution (“E’s contribution”) under a registered pension scheme,
  - (b) conditions A and C in section 196B are met or condition A in section 196C or 196D is met,
  - (c) the asset-backed arrangement is a structured finance arrangement and, accordingly, condition B in section 196B, 196C or 196D (as the case may be) is not met, and
  - (d) there occurs an event (“the relevant event”) –
    - (i) which is not the making of a relevant payment, but
    - (ii) by virtue of which, in accordance with generally accepted accounting practice, the amount of the relevant financial liability is reduced to nil or in part.
- (2) If the relevant financial liability is reduced to nil, Chapter 5B of Part 13 of ITA 2007 or Chapter 2 of Part 16 of CTA 2010 (as the case may be) is no longer to apply in relation to the asset-backed arrangement from when the relevant event occurs.
- (3) In any case, the amount of the reduction of the relevant financial liability mentioned in subsection (1)(d) is treated as follows –
- (a) if E is within the charge to corporation tax when the relevant event occurs, the amount is treated as if it were a profit which E has in respect of E’s loan relationships chargeable to corporation tax under section 299 of CTA 2009 for E’s accounting period in which the relevant event occurs, or
  - (b) otherwise, the amount is treated as if it were an amount of income of E chargeable to income tax under Chapter 8 of Part 5 of ITTOIA 2005 for the tax year in which the relevant event occurs.
- (4) The amount treated as profit or income by subsection (3)(a) or (b) is not to exceed the total amount of relief given in respect of E’s contribution.
- (5) For the purposes of this section –
- (a) “the advance” and “the asset-backed arrangement” have the same meaning as in section 196B, 196C or 196D (as the case may be),
  - (b) “the relevant financial liability” means the financial liability mentioned in section 809BZA(3), 809BZF(3) or 809BZJ(3) of ITA 2007 or section 758(3), 763(3) or 767(3) of CTA 2010 (as the case may be) in respect of the advance,
  - (c) “relevant payment” means a payment which reduces that liability as so mentioned, and
  - (d) the amount of the relevant financial liability before its reduction by virtue of the relevant event and the amount of

the reduction are to be determined in accordance with generally accepted accounting practice.

**196H Employer asset-backed contributions: “advances” under structured finance arrangements**

- (1) This section applies if—
  - (a) an employer pays a contribution under a registered pension scheme,
  - (b) condition A in section 196B, 196C or 196D is met,
  - (c) the asset-backed arrangement is a structured finance arrangement and, accordingly, condition B in section 196B, 196C or 196D (as the case may be) is not met, and
  - (d) the advance gives rise to a loan within the meaning of Chapter 3 (see section 162).
- (2) Section 180(4) does not prevent the advance from being a scheme administration employer payment (if it would otherwise do so).
- (3) For the purposes of this section “the advance” and “the asset-backed arrangement” have the same meaning as in section 196B, 196C or 196D (as the case may be).

**196I Employer asset-backed contributions: supplementary**

- (1) This section applies for the purposes of sections 196B to 196H.
- (2) References to relief being given in respect of a contribution paid by an employer under a registered pension scheme are references to relief being given by way of—
  - (a) the contribution being deducted in computing the amount of the employer’s profits for the purposes of Part 2 of ITTOIA 2005 or Part 3 of CTA 2009 (trading income),
  - (b) the contribution being treated as an expense of management of the employer for the purposes of Chapter 2 of Part 16 of CTA 2009 (expenses of management: companies with investment business), or
  - (c) the contribution being brought into account at Step 1 in section 76(7) of ICTA (expenses of insurance companies) in respect of the employer.
- (3) Whether a person is connected with another person is determined in accordance with section 1122 of CTA 2010.
- (4) “Structured finance arrangement” means an arrangement which is a type 1, type 2 or type 3 finance arrangement for the purposes of Chapter 5B of Part 13 of ITA 2007 or Chapter 2 of Part 16 of CTA 2010 (structured finance arrangements).
- (5) Sections 774 to 776 of CTA 2010 apply as they apply for the purposes of Chapter 2 of Part 16 of that Act.”

2 In section 280(1) of FA 2004 (abbreviations) –

- (a) omit the “and” after the definition of “ITA 2007”, and
- (b) after the definition of “CTA 2009” insert “, and  
“CTA 2010” means the Corporation Tax Act 2010”.

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- 3 (1) The amendment made by paragraph 1 above has effect in accordance with sub-paragraphs (2) to (4); and the amendment made by paragraph 2 above has effect accordingly.
- (2) Sections 196B to 196I of FA 2004 have effect in relation to contributions paid by employers on or after 29 November 2011.
- (3) Section 196G of FA 2004 also has effect in relation to contributions paid by employers before 29 November 2011 where the event mentioned in section 196G(1)(d) occurs on or after that date (and, for the purpose of applying section 196G in relation to such contributions, assume that sections 196B to 196D also have effect in relation to such contributions).
- (4) Section 196H of FA 2004 also has effect in relation to contributions paid by employers before 29 November 2011 (and, for the purpose of applying section 196H in relation to such contributions, assume that sections 196B to 196D also have effect in relation to such contributions).

## PART 2

## TRANSITIONAL PROVISION

*Application and interpretation*

- 4 (1) This Part of this Schedule applies if –
- (a) before 29 November 2011, an employer (“E”) pays a contribution (“E’s contribution”) under a registered pension scheme (“the relevant scheme”),
  - (b) at any time, relief is given in respect of E’s contribution,
  - (c) if the reference in paragraph 3(2) above to 29 November 2011 were instead a reference to the date on which E’s contribution is paid, E would have no entitlement to relief in respect of E’s contribution by virtue of section 196B, 196C or 196D of FA 2004, and
  - (d) the asset-backed arrangement is not completed before 29 November 2011.
- (2) For the purposes of sub-paragraph (1)(c) section 196F of FA 2004 is to be ignored.
- 5 For the purposes of this Part of this Schedule –
- (a) terms used in section 196B, 196C or 196D of FA 2004 (as the case may be) have the same meaning as in that section, and
  - (b) as necessary, assume that section 196B, 196C or 196D of FA 2004 (as the case may be) has effect in relation to E’s contribution.
- 6 (1) This paragraph applies for the purposes of this Part of this Schedule.
- (2) Sub-paragraph (3) applies if the section which would have applied as mentioned in paragraph 4(1)(c) above is section 196B of FA 2004.
- (3) The asset-backed arrangement is “completed” when neither the lender nor any person connected with the lender is any longer entitled under the asset-backed arrangement (conditionally or unconditionally) to payments in respect of the security.
- (4) Sub-paragraph (5) applies if the section which would have applied as mentioned in paragraph 4(1)(c) above is section 196C or 196D of FA 2004.

(5) The asset-backed arrangement is “completed” when the share in the partnership’s profits of the person involved in the relevant change is no longer to be determined under the asset-backed arrangement (conditionally or unconditionally) by reference (wholly or partly) to payments in respect of the security.

- 7 In this Part of this Schedule “the completion day” means –
- (a) the day on which the asset-backed arrangement is to be completed as determined as at the beginning of 29 November 2011, or
  - (b) if earlier, the day on which the asset-backed arrangement is actually completed.

*Certain tax consequences not to have effect*

- 8 (1) This paragraph applies if –
- (a) the section which would have applied as mentioned in paragraph 4(1)(c) above is section 196B of FA 2004, and
  - (b) the asset-backed arrangement would have the relevant effect (ignoring this paragraph).

(2) The asset-backed arrangement is not to have the relevant effect.

- (3) The relevant effect is that –
- (a) an amount of income on which the borrower or a person connected with the borrower would otherwise have been charged to tax is not so charged,
  - (b) an amount which would otherwise have been brought into account in calculating for tax purposes any income of the borrower or of a person connected with the borrower is not so brought into account, or
  - (c) the borrower or a person connected with the borrower becomes entitled to deduct an amount –
    - (i) in calculating income for tax purposes, or
    - (ii) from total income or total profits (as the case may be).

- (4) But if the borrower is a partnership the relevant effect is that –
- (a) an amount of income on which a member of the partnership would otherwise have been charged to tax is not so charged,
  - (b) an amount which would otherwise have been brought into account in calculating for tax purposes any income of a member of the partnership is not so brought into account, or
  - (c) a member of the partnership becomes entitled to deduct an amount –
    - (i) in calculating income for tax purposes, or
    - (ii) from total income or total profits (as the case may be).

(5) In sub-paragraphs (3) and (4) “amount” means an amount which arises on or after 29 November 2011 but on or before the completion day.

- 9 (1) This paragraph applies if –
- (a) the section which would have applied as mentioned in paragraph 4(1)(c) above is section 196C of FA 2004, and
  - (b) any relevant change in relation to the partnership would have the relevant effect (ignoring this paragraph).

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- (2) In such a case –
- (a) Part 9 of ITTOIA 2005 or sections 1259 to 1265 of CTA 2009 (as the case may be) is or are to have effect in relation to the transferor, or any person connected with the transferor, as if the relevant change in relation to the partnership had not occurred, and
  - (b) accordingly, the asset-backed arrangement is not to have the relevant effect.
- (3) The relevant effect is that –
- (a) an amount of income on which the transferor, or the person connected with the transferor, would otherwise have been charged to tax is not so charged,
  - (b) an amount which would otherwise have been brought into account in calculating for tax purposes any income of the transferor, or the person connected with the transferor, is not so brought into account, or
  - (c) the transferor, or the person connected with the transferor, becomes entitled to deduct an amount –
    - (i) in calculating income for tax purposes, or
    - (ii) from total income or total profits (as the case may be).
- (4) In sub-paragraph (3) “amount” means an amount which arises on or after 29 November 2011 but on or before the completion day.
- (5) In deciding whether sub-paragraph (1)(b) is met assume that amounts of income equal to the payments mentioned in section 196C(2)(g) of FA 2004 were payable to the partnership before the relevant change in relation to it occurred.
- 10 (1) This paragraph applies if –
- (a) the section which would have applied as mentioned in paragraph 4(1)(c) above is section 196D of FA 2004, and
  - (b) any relevant change in relation to the partnership would have the relevant effect (ignoring this paragraph).
- (2) The relevant effect is that –
- (a) an amount of income on which a relevant member would otherwise have been charged to tax is not so charged,
  - (b) an amount which would otherwise have been brought into account in calculating for tax purposes any income of a relevant member is not so brought into account, or
  - (c) a relevant member becomes entitled to deduct an amount –
    - (i) in calculating income for tax purposes, or
    - (ii) from total income or total profits (as the case may be).
- (3) A relevant member is a person who –
- (a) was a member of the partnership immediately before the relevant change in relation to it occurred, and
  - (b) is not the lender.
- (4) In sub-paragraph (2) “amount” means an amount which arises on or after 29 November 2011 but on or before the completion day.
- (5) If this paragraph applies –

- (a) Part 9 of ITTOIA 2005 or sections 1259 to 1265 of CTA 2009 (as the case may be) is or are to have effect in relation to any relevant member as if the relevant change in relation to the partnership had not occurred, and
  - (b) accordingly, the asset-backed arrangement is not to have the relevant effect.
- (6) In deciding whether sub-paragraph (1)(b) is met assume that amounts of income equal to the payments mentioned in section 196D(2)(e) of FA 2004 were payable to the partnership before the relevant change in relation to it occurred.

*What happens when the completion day falls?*

- 11 (1) Paragraph 12 or 13 (as the case may be) applies at the end of the completion day.
- (2) For the purposes of paragraphs 12 and 13—
- (a) amount A is the total amount of relief given in respect of E's contribution,
  - (b) amount B is the total of the following amounts—
    - (i) any amounts of income which are charged to tax by virtue of paragraph 8, 9 or 10 above (as the case may be),
    - (ii) any amounts brought into account in calculating income for tax purposes by virtue of paragraph 8, 9 or 10 above (as the case may be) (so far as not reflected in sub-paragraph (i)), and
    - (iii) any amounts stopped from being the subject of an income deduction by virtue of paragraph 8, 9 or 10 above (as the case may be) (so far as not reflected in sub-paragraph (i) or (ii)), and
  - (c) amount C is the amount of the payment mentioned in sub-paragraph (5) or (7) (as the case may be) so far as the payment—
    - (i) is made under the asset-backed arrangement on the completion day,
    - (ii) is not reflected in amount B,
    - (iii) is not the subject of an income deduction, and
    - (iv) is not a contribution paid by E under the relevant scheme but nevertheless becomes (directly or indirectly) part of the sums held for the purposes of the relevant scheme.
- (3) In sub-paragraph (2) “income deduction” means a deduction to which any person is entitled—
- (a) in calculating income for tax purposes, or
  - (b) from total income or total profits.
- (4) Sub-paragraph (5) applies if the section which would have applied as mentioned in paragraph 4(1)(c) above is section 196B of FA 2004.
- (5) The payment referred to in sub-paragraph (2)(c) is the payment (if any) which the borrower, or a person connected with the borrower, makes to the lender, or a person connected with the lender, in order to acquire—
- (a) the security, or
  - (b) any asset substituted for the security under the asset-backed arrangement.



- (6) Sub-paragraph (7) applies if the section which would have applied as mentioned in paragraph 4(1)(c) above is section 196C or 196D of FA 2004.
- (7) The payment referred to in sub-paragraph (2)(c) is the payment (if any) which E, or a person connected with E, makes to the lender, or a person connected with the lender, in order to reverse the relevant change in relation to the partnership.
- 12 (1) This paragraph applies if amount A exceeds the sum of amounts B and C.
- (2) The amount of the excess is treated as follows –
- (a) if E is within the charge to corporation tax on the completion day, the amount is treated as if it were a profit which E has in respect of E's loan relationships chargeable to corporation tax under section 299 of CTA 2009 for E's accounting period in which the completion day falls, or
  - (b) otherwise, the amount is treated as if it were an amount of income of E chargeable to income tax under Chapter 8 of Part 5 of ITTOIA 2005 for the tax year in which the completion day falls.
- 13 If the sum of amounts B and C exceeds amount A –
- (a) E is to be treated as having paid a contribution under the relevant scheme in respect of any individual of an amount equal to the excess,
  - (b) the contribution is to be treated as having been paid on the completion day, and
  - (c) E is to be given relief as provided for by section 196 of FA 2004 accordingly.

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## EXPLANATORY NOTE

### EMPLOYER ASSET-BACKED PENSION CONTRIBUTIONS

#### SUMMARY

1. This clause and Schedule amend Part 4 of Finance Act (FA) 2004 as it relates to employer pensions tax relief by inserting a number of new sections into FA 2004 as well as providing transitional provisions in order to ensure that the amount on which relief is given in respect of a contribution paid by any employer accurately reflects, but does not exceed, the payments received by the registered pension scheme. These changes have effect from 29 November 2011.
2. Specifically, the Schedule will apply to asset-backed contribution (ABC) arrangements used by some employers to fund their registered pension schemes.
3. An ABC arrangement involves the offset of an employer's legal obligation to pay a pension contribution against the registered pension scheme's legal obligation to purchase an asset from the employer directly or indirectly, using the contribution (there are also ABC arrangements that involve an upfront monetary contribution).
4. These types of arrangement enable an employer, or a person connected with the employer (hereafter referred to as "the employer etc"), to provide for payments over a period of time (or an income stream) to the pension scheme. A more complex ABC arrangement typically involves a special purpose vehicle (for example, a partnership of which the employer is a member (an employer-related partnership)), in which case the employer provides the pension scheme with the income stream indirectly through the vehicle. The income stream is derived from assets of the employer or a connected party including an employer-related partnership.

#### DETAILS OF THE SCHEDULE

5. Part 1 inserts new sections 196B to 196I after section 196A FA 2004.
6. Part 2 (paragraphs 4-13) introduces transitional provisions for pre-commencement ABC arrangements where the contribution was paid before 29 November 2011 and the structured finance arrangement (SFA) rules<sup>1</sup> do not apply. For pre-commencement arrangements that are SFAs, the tax treatment does not change on 29 November 2011 and the only "transitional" provision is new section 196G (see below).

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<sup>1</sup> The SFA rules are set out in Part 16 of Corporation Tax Act 2010 (for corporation tax purposes) and Part 13 of Income Tax Act 2007 (for income tax purposes).

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### Part 1 – sections 196B to 196I and paragraphs 2-3

7. The new provisions in Part 1 follow the design of the structured finance legislation which applies where a person enters into a “structured finance agreement”. A structured finance arrangement (SFA) is an arrangement where in accordance with generally accepted accounting practice, a person (the borrower) records in the borrower’s accounts a financial liability in respect of a sum (the advance) paid by “the lender”, and the advance will be repaid by an income stream.
8. In the case of ABC arrangements, the obligations of the employer and the registered pension scheme as described above give rise to a situation similar to a SFA, where the employer etc or an employer-related partnership or other relevant person is “the borrower”, receives money or another asset (the advance) from the pension scheme (the lender). The advance is wholly or partly funded out of the employer’s contribution and the lender is entitled to a series of payments in respect of the borrower’s asset (the security).
9. The main provisions (new sections 196B to 196D) will deny pensions tax relief (upfront relief) to the employer on the contribution paid using the ABC arrangement if the SFA rules do not apply. Instead deductions against the profits or income of the employer will be given in respect of each payment that the employer makes to the pension scheme (the lender) directly or indirectly under the income stream (“pay as you go” relief). Amounts of an income stream, which were previously taxable in the hands of the employer, are likely to cease to be taxable upon the transfer of the income stream to the lender or a connected person (the lender etc).
10. There are also revenue protection provisions (new sections 196F and 196G) - an anti-avoidance provision to prevent any employer from securing tax relief that exceeds the value made to the pension scheme and a separate provision to recover relief given to an ABC arrangement that falls within the SFA rules when the financial liability is later reduced by an event other than the making of payments.
11. A series of new provisions – new sections 196E, 196H and 196I – provide for supplementary provisions and application. Paragraph 2 makes a consequential change and paragraph 3 makes provision for commencement of the new provisions.

### The simple case – new section 196B

12. New section 196B deals with the simple case where the employer etc is the borrower and the lender is a person who acts for, or is otherwise connected with the registered pension scheme. It stipulates in sub-section 1 the conditions under which relief under section 196 FA 2004 (upfront relief) will **not** be given to the employer (the

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borrower) in respect of a contribution paid under the ABC arrangement.

13. New sections 196B(2), (4) and (5) set out these conditions as follows:
  - Condition A is that -
    - the borrower (employer etc) receives the advance which is wholly or partly paid or provided by the lender etc out of the contribution in respect of the arrangement;
    - the borrower or a person connected with the borrower (borrower etc) disposes of an asset (the security) to or for the benefit of the lender etc; and
    - the lender etc is entitled to payments in respect of the security.
  - Condition B is that the arrangement is **not** a SFA as defined in new section 196I(4); and
  - Condition C is that it is reasonable to suppose, that the amount of one or more of the payments mentioned above is determined (wholly or partly) on the basis that, in essence, some part of the advance represents a loan (including any advance of money in accordance with new section 196B(7)(c)) which is to be repaid by the payment(s).
14. New section 196B(2) also makes it clear that those arrangements that fall within new section 196C(2) and 196D(2) do not fall within new section 196B(2).
15. New section 196B(3) states that condition A is met even if an entitlement of the lender etc is subject to any condition.
16. New section 196B(6) makes it clear that condition C is met even if repayments of the loan might be subject to any condition, or that the accounts of any person do not record a financial liability in respect of the advance or is not otherwise treated as representing a loan for the purposes of the accounts of any person. However, subject to that, all relevant circumstances are to be taken into account in order to get to the essence of the matter.
17. New section 196B(7)(a) ensures that references to a person connected with the borrower or lender do not include the lender or borrower respectively. This means that new section 196B cannot be triggered accidentally just because the borrower and lender are connected. New section 196B(7)(b) ensures that if the borrower is not the employer, the reference to a person connected to the borrower includes a person connected with the employer who would not otherwise be connected with the borrower.

**The complex case – new sections 196C and 196D**

18. New sections 196C and 196D deal with complex types of ABC arrangement involving a partnership receiving the advance, and changes in profit sharing arrangements in relation to the lender etc.
19. New section 196C will apply where, as part of the ABC arrangement which is used to make the contribution, the employer etc (the transferor) transfers an asset to a partnership and is a member of that partnership immediately after the transfer (whether or not a member immediately before the transfer), and the lender (the pension scheme) becomes a member of the partnership at any time as set out in new section 196E. In that circumstance, new section 196C(1) provides that the employer will **not** receive upfront tax relief under section 196 FA 2004 in respect of the contribution paid to the registered pension scheme when conditions A and B are met.
20. New sections 196C(2) and (5) set out these conditions as follows:
  - Condition A is that -
    - the transferor is the employer etc;
    - the transferor or a person connected with the transferor (transferor etc) disposes of the security to a partnership and is a member of the partnership immediately after the disposal
    - the partnership receives the advance, which is wholly or partly paid or provided out of the employer's contribution, from a person (the lender) other than the transferor;
    - there is a relevant change in relation to the partnership as set out in new section 196E; and
    - the share in the partnership's profits of the person involved in the relevant change is determined by reference to payments in respect of the security.
  - Condition B is that the arrangement is **not** a SFA as defined in new section 196I(4).
21. New section 196C(3) ensures that where the transferor is not the employer, the reference to a person connected to the transferor includes a person connected with the employer who would not otherwise be connected with the transferor.
22. New section 196C(4) provides that condition A is met even if the determination of the share of partnership's profits is subject to any condition.
23. New section 196D will apply where the ABC arrangement which the employer uses to make the contribution to the pension scheme also involves a partnership receiving the advance but the security is held by a pre-existing partnership. As part of the ABC arrangement, the partnership receives an advance that is funded in some way by the employer's contribution. In that circumstance, new section 196D(1) provides that the employer will **not** receive upfront tax relief under

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section 196 FA 2004 in respect of the contribution paid to the registered pension scheme under the ABC arrangement when conditions A and B are met.

24. New sections 196D(2) and (4) set out these conditions as follows:
- Condition A is that -
    - a partnership holds the security at any time before the ABC arrangement is made;
    - the partnership receives the advance which is wholly or partly paid or provided by the lender out of the employer's contribution in respect of the arrangement;
    - there is a relevant change in relation to the partnership as set out in new section 196E; and
    - the share in the partnership's profits of the person involved in the relevant change is determined by reference to payments in respect of the security.
  - Condition B is that the arrangement is **not** a SFA as defined in new section 196I(4).
25. New section 196D(3) provides that condition A is met even if the determination of the share of partnership's profits is subject to any condition.
26. New section 196E provides that a relevant change in relation to the partnership occurs (which in turn enables the conditions in new sections 196C and 196D to be met) if one of the conditions - condition X or condition Y - is met. New sections 196E(2) and (3) set out these conditions as follows:
- Condition X is that the lender etc joins the partnership in connection with the ABC arrangement at any time; or
  - Condition Y is that there is a change in the lender etc's share of the partnership's profits in connection with the asset-backed arrangement.
27. References used in this new section and in new sections 196C and 196D are explained in new sections 196E(4) and (5).

### **Anti-avoidance – new section 196F**

28. New section 196F is an anti-avoidance provision to deny upfront relief or recover any relief already given when the employer etc sets up an arrangement (the avoidance arrangement) mainly for the purpose of securing tax relief that will exceed the amount the employer should receive relative to the total amount of payments the employer will make to the pension scheme under the ABC arrangement. This provision will only apply to ABC arrangements where the contribution is paid on or after 29 November 2011.

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29. New section 196F(1) provides that this new provision applies where upfront relief for the ABC arrangement is not denied under new sections 196B, 196C, or 196D because the arrangement is a SFA and the employer etc enters into the avoidance arrangement.
30. New section 196F(2) provides that where the avoidance arrangement is entered into at or before the time when the advance referred to in new sections 196B, 196C or 196D is received, upfront relief is denied on the contribution paid under the ABC arrangement by deeming that Condition B in one of those sections is met.
31. New section 196F(3) provides that where the avoidance arrangement is entered into after the advance is received, then the amount of the relevant financial liability at the time the avoidance arrangement is entered into is treated as profit or income that is charged to the employer for the period in which that time falls.
32. New section 196F(4) sets out that the amount treated as profit or income is not to exceed the total amount of relief given to the employer in respect of the ABC arrangement. The terms used in this new section are defined in new section 196F(5).

### **Relief recovery due to accounting changes – new section 196G**

33. New section 196G is a new provision to recover upfront relief given to an ABC arrangement (including a pre-commencement arrangement) that falls within the SFA rules when the financial liability is later reduced by an event other than the making of payments. This provision applies to this type of ABC arrangement where the contribution is paid before and after 29 November 2011 but in the case of pre-commencement arrangements, it only applies where the event occurs on or after that date.
34. New section 196G(1) provides that the section applies where the ABC arrangement is a SFA, and an event, other than the making of payments to the pension scheme, occurs which results in the advance (or part of it) no longer being recorded as a financial liability in the employer's (or partnership's) accounts.
35. If the financial liability is reduced to nil, the ABC arrangement will cease to be a SFA under new section 196G(2).
36. New section 196G(3) provides that the amount of the reduction in the relevant financial liability immediately before this event will be treated as profit or income chargeable on the employer in the period in which the event occurs.
37. New section 196G(4) provides that the amount treated as profit or income under new sub-section 3 cannot exceed the total amount of relief already given to the employer in respect of the arrangement.

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The terms used in new section 196G are defined under new section 196G(5).

### **Treatment of advances that fall within the SFA rules – new section 196H**

38. New section 196H provides that any advance under an ABC arrangement which is a SFA and gives rise to a loan within the meaning of Chapter 3 of FA 2004 is not prevented from meeting the definition of a scheme administration employer payment in S180 FA 2004 regardless of whether the advance also meets the definition of a loan for the purposes of FA 2004. This means that no unauthorised payment charge will arise under section 208 FA 2004 purely by virtue of the fact that the advance gives rise to a loan which is not capable of meeting the conditions of section 179 FA 2004.

### **Supplementary provisions and application – new section 196I and paragraphs 2**

39. New section 196I provides a number of definitions and other supplementary provisions for new sections 196B to 196H.
40. New section 196I(2) explains the references to relief being given in respect of a contribution paid by an employer under a registered pension scheme.
41. New section 196I(3) refers to the meaning of connected persons in section 1122 Corporation Tax Act (CTA) 2010.
42. New section 196I(4) explains the references to a SFA are to the definition of a type 1, type 2 or type 3 arrangement under Part 13 of the Income Tax Act (ITA) 2007 (for income tax purposes) or Part 16 of CTA 2010 (for corporation tax purposes).
43. New section 196I(5) provides that sections 774 (accounts), 775 (arrangements) and 776 (assets) of CTA 2010 apply to new sections 196B to 196H in the same way as they do for the purposes of Part 16 of CTA 2010.
44. Paragraph 2 make a consequential amendment to section 280(1) FA 2004 (abbreviations) by inserting a reference to CTA 2010.

### **Commencement and application of new sections 196B to 196I – paragraph 3**

45. Paragraphs 3(1) and (2) provide that the amendments made by new sections 196B to 196I shall have effect for contributions paid by employers on or after 29 November 2011.
46. Paragraph 3(3) provides that new section 196G also has effect for contributions paid before 29 November 2011 where the relevant event as described in new section 196G(1)(d) occurs on or after 29



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November 2011. Where this paragraph applies, new sections 196B to 196D also have effect for the purpose of applying new section 196G.

47. Paragraph 3(4) provides that new section 196H also has effect for contributions paid before 29 November 2011 and assumes that new sections 196B to 196D have effect in relation to these contributions for the purposes of applying new section 196H.

### **Part 2 - Transitional rules (paragraphs 4 to 13)**

48. Part 2 contains transitional provisions which apply the “relevant effects” of the SFA rules to any pre-commencement ABC arrangement that does not fall within the SFA rules. These rules apply to income amounts or payments made on or after 29 November 2011. There are also rules for introducing a mechanism to make a tax adjustment at the end of any of these arrangements which ensures the employer receives tax relief in respect of the total amount of payments made to the pension scheme under the ABC arrangement.
49. The only “transitional” provision that will apply to pre-existing ABC arrangements which are SFAs is new section 196G. This section recovers any excess of relief given where the relevant event occurs on or after 29 November. Further detail can be found in the last part of this explanatory note concerning new section 196G and is not repeated in this part of the note.

#### Detail of transitional rules

##### *Paragraphs 4 to 7 – application and interpretation*

50. Paragraphs 4-7 provide for application and interpretation of the terms used in Part 2.
51. Paragraph 4 provides that transitional provisions will apply where an ABC arrangement with the contribution paid before 29 November 2011 would **not** have received relief under new sections 196B to 196D had the contributions been paid on or after 29 November 2011 and the arrangement is not ‘completed’ as determined under paragraph 6 before that date.
52. Paragraph 5 provides that for the purposes of Part 2, the terms used in new sections 196B to 196D have the same meaning as in those new sections and where necessary it is assumed that those new sections have effect in relation to the employer’s contribution.
53. Paragraph 6 provides that an ABC arrangement that would be denied upfront relief under section 196B, 196C or 196D had the contribution been paid on or after 29 November 2011 is completed if :
- where the arrangement is a simple case, the lender etc is no longer entitled to payments in respect of the security; or

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- where the arrangement is a complex case, the share in the partnership's profits of the person involved in the relevant change is no longer to be determined by reference to payments in respect of the security.
54. Paragraph 7 provides that 'the completion day' is the day on which the ABC arrangement is to be completed as determined as at the beginning of 29 November 2011 or the actual day if earlier. This prevents the employer seeking to extend the duration of the arrangement to avoid the transitional provisions set out in paragraphs 11 to 13.

### *Paragraphs 8 to 10 – certain tax consequences not to have effect*

55. Paragraphs 8-10 deem the relevant ABC arrangements not to have "the relevant effect" as set out in paragraphs 8(3), 9(3) and 10(2). This means that on or after 29 November 2011, no deduction will be given to any income payments that the borrower (the employer or a connected party or other relevant person) makes to the lender etc under the ABC arrangement and any income amounts that have been transferred to the lender etc will be brought back into tax charge on the employer etc or other relevant person.
56. Paragraph 8(1) provides that paragraph 8 applies to ABC arrangements where, had the employer's contribution been paid on or after 29 November 2011, new section 196B would have applied so that the arrangement would have the "relevant effect". The "relevant effect" defined in paragraph 8(3) is that the borrower etc (the employer etc) would receive relief for payments to the lender etc (the pension scheme) made under the arrangement either by way of an income deduction or by an income amount which would otherwise have been charged to tax not being so charged.
57. Paragraph 8(2) deems the arrangement **not** to have the "relevant effect" which is set out in paragraph 8(3). This means that either no relief will be given for any income payments the borrower etc (the employer etc) makes to the lender etc (the pension scheme) under the ABC arrangement or any income amounts that would have been charged to tax if not for the ABC arrangement will be brought back into tax as a charge on the employer etc.
58. Paragraph 8(4) defines the relevant effect if the borrower is a partnership.
59. Paragraph 8(5) provides that "amount" in sub-paragraphs 3 and 4 means an amount that arises on or after 29 November 2011 but on or before the completion day as set out in paragraph 7. This means that before the completion day, this paragraph prevents relief for income payments made on or after 29 November 2011 or brings back income amounts into charge from that date.

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60. Paragraph 9(1) provides that paragraph 9 applies to ABC arrangements where, had the employer's contribution been paid on or after 29 November 2011, new section 196C would have applied so that the ABC arrangement would have the "relevant effect". The "relevant effect", defined in paragraph 9(3), is that the transferor etc (the employer etc) would receive relief either by way of an income deduction or by an amount which would otherwise have been charged to tax not being so charged.
61. Paragraph 9(2) deems the arrangement **not** to have the "relevant effect". This means that either no relief will be given for any income payment made by the partnership to the lender etc (the pension scheme) under the arrangement or any amount that would have been charged to tax if not for the ABC arrangement will be brought back into tax as a charge on the transferor etc (the employer etc).
62. Paragraph 9(4) provides that for the purposes of sub-paragraph 3, "amount" means an amount that arises on or after 29 November 2011 but on or before the completion day as set out in paragraph 7. This means that before the completion day, this paragraph prevents relief for income payments made on or after 29 November 2011 or brings back income amounts into charge from that date.
63. Paragraph 9(5) provides that in determining whether the ABC arrangement would have the relevant effect, it is to be assumed that the amounts of income equal to the payments mentioned in new section 196C(2)(g) were payable to the partnership before the relevant change occurred.
64. Paragraphs 10(1) provides that paragraph 10 applies to ABC arrangements where had the employer's contribution been paid on or after 29 November 2011, new section 196D would have applied so that the ABC arrangement would have the "relevant effect". The "relevant effect", defined in paragraph 10(2), is that the "relevant member" would receive relief by way of an income deduction or by an income amount which would otherwise have been charged to tax not being so charged.
65. Paragraph 10(3) provides that a "relevant member" is a person who was a member of the partnership immediately before the relevant change in the partnership occurred and the person is not the lender.
66. Paragraph 10(4) provides that for the purposes of paragraph sub-paragraph 2, "amount" means an amount that arises on or after 29 November 2011 but on or before the completion day as set out in paragraph 7. This means that before the completion day, this paragraph prevents relief for income payments made on or after 29 November 2011 or brings back income amounts into charge from that date.

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67. Paragraph 10(5) deems the arrangement **not** to have the “relevant effect” as set out in paragraph 10(2). This means no relief will be given for any income payments made from the partnership to the lender (the pension scheme) or any income amounts that would have been charged to tax if not for the ABC arrangement will be brought back into tax as a charge on the relevant member (the employer etc or other relevant person).
68. Paragraph 10(6) provides that in determining whether the ABC arrangement would have the relevant effect, it is to be assumed that the amounts of income equal to the payments mentioned in new section 196D(2)(e) were payable to the partnership before the relevant change occurred.

### *Paragraphs 11 to 13 – what happens when the completion day falls?*

69. Paragraphs 11-13 provides for a tax adjustment on the employer when the ABC arrangement ends to ensure that the total amount on which relief is given to the employer will accurately reflect, but will not exceed the total amount of payments actually given to the pension scheme under the arrangement.
70. This adjustment mechanism will take into account not just all the payments actually made to the pension scheme but also all the relief in the form of deductions against taxable profits or income given to the employer before and after 29 November 2011. Any deductions and payments given before 29 November 2011 will be cancelled out in the overall adjustment so the amounts set out in paragraphs 11 to 13 do not include these sums. The adjustment can result in either a charge on the employer or further tax relief.
71. The following example that uses the facts as set out in Example 3 in the consultation document, *Employer Asset-backed Pension Contributions*<sup>2</sup> published on 24 May 2011 on both the HMRC and HM Treasury websites, and illustrates how the adjustment mechanism as set out in paragraphs 11-13 works.

### Example

The ABC arrangement does not fall within the SFA rules.

Pension scheme deficit = £400m

Contribution paid under the ABC arrangement = £400m

Yearly payment = £22.5m (of which £2.5m could be a finance charge if the arrangement were a SFA) payable for 20 years.

Two payments were made before 29 November 2011.

Assume that the employer company is profitable throughout the entire course of the ABC arrangement.

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<sup>2</sup> <http://www.hmrc.gov.uk/budget-updates/march2011/index.htm#24may>

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Using amounts A, B and C as defined in paragraph 11(2),

Amount A (relief for E's contribution) = £400m

Amount B (total amount of denied ongoing payments under paragraph 8, 9 or 10) = £405m (including the last payment at year 20)

Amount C = 0 (as the last payment falls within the meaning of "income deduction" and so paragraph 11(2)(c)(ii) is not met)

Assume there is an amount D (not included in this Schedule) = pre-commencement relief = pre-commencement payments = £22.5m x 2 years = £45m

Amount A – (Amount B + Amount C) = £5m on which additional relief arises under paragraph 13 of the new legislation.

So the total relief to the employer = Amount A (£400m) + Amount D (£45m) + the adjustment relief (£5m) = £450m

Total payments received by the pension scheme = Amount D + Amount B = £45m + £405m = £450m which equals to the total relief.

This means that the employer relief accurately reflects the payments actually received by the pension scheme.

72. Paragraph 11(1) provides that either paragraph 12 or 13 will apply at the end of the completion day of the arrangement as defined in paragraph 7.
73. Paragraph 11(2) defines amount A, amount B and amount C for any tax adjustment as set out in paragraphs 12 and 13:
- amount A is the total amount of relief given in respect of the employer's contribution paid under the ABC arrangement;
  - amount B is the total of any amounts in respect of which the employer has been denied relief under paragraphs 8, 9 or 10. These are the payments for which a deduction has been denied or the amounts brought back to charge on the employer etc or other relevant person; and
  - amount C is the amount of the payment made under the ABC arrangement before the completion day which is not reflected in amount B, is not the subject of an income deduction and is not a contribution paid by the employer to the pension scheme but becomes part of the sums held by the pension scheme.
74. Paragraph 11(3) defines "income deduction" for the purposes of sub-paragraph 2.
75. Paragraphs 11(4) and (5) provide that where, had the employer's contribution been paid on or after 29 November 2011, new section

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- 196B would have applied, amount C is the payment (if any) which the borrower etc makes to the lender etc in order to acquire the security or an asset in place of the security under the ABC arrangement.
76. Paragraphs 11(6) and (7) provide that where, had the employer's contribution been paid before 29 November 2011, new sections 196C or 196D would have applied, amount C is the payment (if any) which the employer etc makes to the lender etc in order to reverse the relevant change in relation to the partnership.
77. Paragraph 12 provides that if at the end of the completion day, the amount of tax relief given to the employer in respect of the contribution paid under an ABC arrangement is greater than the total amount of payments made to the pension scheme, then the excess tax relief in the form of the difference between the two amounts will be recovered from the employer.
78. Paragraphs 12(1) and (2) provide that where amount A is greater than the sum of amount B and amount C, the excess will be either treated as a profit or income arising on the employer in the period of accounts<sup>3</sup> in which the completion day falls.
79. Paragraph 13 provides that that if at the end of the completion day, the amount of tax relief given to the employer in respect of the contribution paid under the ABC arrangement is less than the total amount of payments made to the scheme, then the employer will be entitled to additional relief. Where the sum of amount B and amount C exceeds amount A, the excess is treated as an employer contribution paid on the completion day to which the employer is to be given to relief in accordance with section 196 FA 2004.

### BACKGROUND NOTE

80. This Schedule limits the amounts on which tax relief will be given to an employer in respect of a contribution paid under an asset-backed arrangement so that the relief accurately reflects, but does not exceed, the total amount of payments made to the registered pension scheme.
81. It does not apply to any straightforward monetary sum that a sponsoring employer gives to the registered pension scheme as a pension contribution or any employer's transfer of an asset to the pension scheme which is unconditional or outright so that the pension scheme gains complete ownership of the asset on an irrevocable basis. In these cases, relief will continue to be given to the employer in respect of the contribution paid under section 196 in Finance Act 2004 provided that the requirements of that section are met.

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<sup>3</sup> The relevant period of accounts is either (a) the relevant accounting period if the employer etc is a company or (b) the relevant tax year if the employer etc is an unincorporated business.

## FINANCE BILL

82. At Budget 2011, the Government announced that it would consult on changing tax rules to prevent unintended and excessive relief arising from employer asset-backed pension contributions, while preserving as much flexibility as possible for employers and their pension schemes to use these contributions, as well as ensuring that the compliance process is deliverable for Government without creating undue burdens on HM Revenue & Customs or customers.
83. A consultation document, ‘Employer Asset-backed Pension Contributions’ was published on 24 May 2011 and the consultation closed on 16 August 2011. The document invited views on two broad options: (a) providing upfront relief to the employer only for giving a monetary contribution or a cash-convertible asset to the pension scheme, and (b) providing either upfront relief or “pay as you go” relief depending on whether the asset-backed arrangement would fall within the structured finance legislation. The main purpose of the consultation was to establish which option would better meet the Government’s objectives (see paragraph 82) while also ensuring that pensions tax relief would remain fair and sustainable in the long term.
84. Following the consultation, legislation has been published, which is designed on the basis of the second option above and informed by responses to and information received during the consultation. In order to prevent certain activity or behaviour in relation to these types of arrangement which brings a significant risk to the Exchequer, legislation has effect from 29 November 2011, which is the date of the publication of the legislation and this explanatory note.
85. Further detail is included in the autumn statement, the written ministerial statement, the summary of responses document and the Tax Information and Impact Note, which have all been published on 29 November 2011.
86. If you have any questions about this change, please contact Windy Kwok on 020 7147 2835 (email: [Windy.Kwok@hmrc.gsi.gov.uk](mailto:Windy.Kwok@hmrc.gsi.gov.uk)) or Richard Rogers on 020 7147 2625 (email: [Richard.Rogers@hmrc.gsi.gov.uk](mailto:Richard.Rogers@hmrc.gsi.gov.uk)). Enquiries can also be sent to: [pensions.policy@hmrc.gsi.gov.uk](mailto:pensions.policy@hmrc.gsi.gov.uk)