

REPORT OF THE GROUP DIRECTOR, FINANCE & CORPORATE RESOURCES

Voluntary Scheme Pays Policy 2018 Pensions Committee 23rd July 2018	Classification Public	Enclosures One.
	Ward(s) affected ALL	

1. INTRODUCTION

- 1.1 This report introduces the first 'Voluntary Scheme Pays Policy 2018', which has been drafted as a discretionary option for members of the Local Government Pension Scheme who breach HMRC's annual allowance limit on pension savings growth in a financial year, and to agree the policy permitting members to use 'Voluntary Scheme Pays' and the circumstances for accepting such applications.

2. RECOMMENDATION**2.1 Pensions Committee is recommended to:**

- **Approve the Voluntary Scheme Pays Policy 2018**

3. RELATED DECISIONS

- 3.1 None

4. COMMENTS OF THE GROUP DIRECTOR, FINANCE AND CORPORATE RESOURCES

- 4.1 Allowing scheme members to exercise their right to request an Annual Allowance Charge to be paid via 'Voluntary Scheme Pays' will result in additional administration, although the amount of members that might wish to exercise this right is expected to be of a low volume.
- 4.3 Guidance on the calculation of the reduction in pension benefits following a Scheme Pays election has been issued by the Secretary of State for Communities and Local Government in conjunction with consultation by Government Actuaries Department (GAD) in order to ensure that the Scheme Pays offset is cost neutral to the scheme

5. COMMENTS OF THE DIRECTOR OF LEGAL AND GOVERNANCE

- 5.1 There is no statutory requirement for an Administering Authority to agree to Voluntary Scheme Pays requests so it is therefore for each authority to determine its policy on policy. However, it would seem best practice having robust governance arrangements in place, to facilitate informed decision making, supported by appropriate advice, policies and strategies, whilst ensuring compliance with appropriate legislation and statutory guidance. Thereby ensuring management of the Fund is done in a fair and equitable manner, having regard to what is in the best interest of the Fund's stakeholders, particularly the scheme members and employers.
- 5.2 There are no immediate legal implications arising from this report.

6. BACKGROUND

- 6.1 Annual Allowance is one of the limits set by the Government in relation to the level of an individual's pension savings, known as pension input, before a charge becomes due to HM Revenue and Customs (HMRC).
- 6.2 Scheme members are normally required to pay their tax charges directly to HMRC, however, where the annual allowance charge in a tax year exceeds £2,000, members are able to elect to meet some or all of the tax charge from their future pension benefits. This is known as the Mandatory Scheme Pays option. This option requires the Pension Fund to pay the tax charge on the member's behalf and then to reduce their future pension benefits accordingly.
- 6.4 Local Government Pension Scheme (LGPS) administering authorities now have the power to grant a member's request to pay their annual allowance charge even if they do not meet the criteria for MSP; this mechanism has become known as Voluntary Scheme Pays (VSP).
- 6.5 Voluntary Scheme Pays is where the scheme member's annual allowance tax charge is less than £2,000, and the member may ask the Pension Fund to pay their annual allowance tax charge on a voluntary basis via the Voluntary Scheme Pays option with a corresponding reduction to their LGPS benefits. This would include those members adversely affected by HMRC's tapering rule. This, however, is subject to the Administering Authority's approval which is discretionary.
- 6.6 An important consideration however is that, in the tax year 2016/17, HMRC amended the annual allowance rules by introducing the tapered annual allowance for employees with taxable income in excess of £150,000 (including the value of the employer's pension contribution). For every £2 of income over £150,000 the standard annual allowance is reduced by £1. However, this is subject to a minimum reduced annual allowance of £10,000.

7. THE POLICY

- 7.1 As it currently stands, Scheme members whose pension growth in a year breaches the Mandatory Scheme Pays limit have only the following options –
- Pay the tax charge directly to HMRC
 - Opt for Mandatory Scheme Pays for breach over £40,000
 - If agreed opt for Voluntary Scheme Pays for the amount below £40,000
- 7.2 Where the member's annual allowance has been reduced to £10,000, they would have no option other than to pay a potentially significant tax charge directly to HMRC on the amount between £40,000 and their tapered annual allowance, i.e. £30,000.
- 7.3 HMRC have introduced different timelines for payment of the tax charges between Mandatory and Voluntary Scheme Pays:

Mandatory Scheme Pays - The deadline for members who incur a tax charge and wish to apply to the pension fund to utilise Mandatory Scheme Pays is 31 July each year. The subsequent deadline for administering authorities to make the payment to HMRC is the following 14 February.

Voluntary Scheme Pays – There is technically no deadline for members to request to use the Voluntary Scheme Pays option. However, subject to the administering authority's approval, the tax charge payment to HMRC must be made before 31 January in the following tax year to ensure additional interest charges are not incurred by the member.

7.4 The Fund **will** accept applications for Voluntary Scheme Pays in the following circumstances:

- A member is subject to the Tapered Annual Allowance or the Money Purchase Annual Allowance and has a tax charge of more than £2,000 relating to input in the London Borough of Hackney Pension Fund, and the irrevocable election is received by 31st December following the end of the tax year in which the input arises (i.e. 31st December 2018 for input in the 2017/18 year).
- A member meets all the criteria for Mandatory Scheme Pays but was unable to meet the 31st July deadline due to an administrative error or omission by the Hackney Pension Fund and/or the administrators Equiniti (i.e. the member was not notified of their pension input in time for them to meet the deadline). In these circumstances the application for Voluntary Scheme Pays should be made within 2 months of the member receiving notification of their pension input.

7.5 The Fund **will not** accept applications for Voluntary Scheme Pays in the following circumstances:

- The member's tax charge relating to pension input in the LGPS in England & Wales is less than £2,000, but they have applied for Voluntary Scheme Pays because their total tax charge when taking input from other arrangements into account is more than £2,000.
- The member has a Mandatory Scheme Pays right in respect of pension input in the LGPS in England and Wales, but has also asked the Fund to pay a tax charge relating to input in a separate pension arrangement.
- The member's tax charge is less than £2,000.
- A member did not meet the 31st July deadline for applying for Mandatory Scheme Pays, and this failure to meet the deadline was **not** due to any administrative error or omission by Hackney Pension Fund or by the pension administrators.

7.6 A Voluntary Scheme Pays request in any other scenario will be considered by the Fund on its merits; on a case by case basis. Following the acceptance of an election for Voluntary Scheme Pays, the member's benefits will be reduced by an amount corresponding to the tax charge paid by the Fund, using the guidance issued by the Government Actuary's Department (GAD).

7.7 The Voluntary Scheme Pays option could be utilised to the benefit of the Hackney Pension Fund as it is more likely the member will remain in the scheme and continue contributing to the Fund. The alternative would be for the member to leave the

scheme to avoid incurring the tax charge thus reducing available funds in the scheme. This could impact on Scheme members down to middle manager levels with long service and could impact on Scheme Employers ability to attract and retain employees in key roles.

- 7.8 Once the policy is approved by the Pensions Committee it will be effective immediately. It will be formally reviewed and updated at least every 3 years or sooner, if there are any changes to the LGPS or other relevant Regulations or Guidance which need to be taken into account.

List of Appendices

Appendix 1 - London Borough of Hackney Pension Fund, Voluntary Scheme Pays Policy 2018

Ian Williams
Group Director
Finance & Corporate Resources

Report Originating Officers: Julie Stacey ☎020-8356 3565
Financial considerations: Michael Honeysett ☎020-8356 3332
Legal comments: Patrick Rodger ☎020-8356 6187