Low Incomes Tax Reform Group

A voice for the unrepresented

Finance Bill 2017-19
Money purchase annual allowance, clause 7
Briefing from the Low Incomes Tax Reform Group (LITRG)

1 Summary

1.1 Once a person has accessed pension savings flexibly, if they wish to pay anything further to a defined contribution pension, tax-relieved contributions are restricted to the money purchase annual allowance (MPAA). Up to 5 April 2017, the MPAA is £10,000. From 6 April 2017, clause 16 reduces it to £4,000.

1.2 The reduction in the MPAA is designed to further limit individuals who have already accessed pension savings to recycle this cash back into pensions and thereby benefit from tax relief for a second time.

1.3 LITRG is concerned that some people might unwittingly be caught out by the change. In consultation, we asked for two key safeguards:

1.3.1 the level of the MPAA should be kept under review; and

1.3.2 the taxpayer should be able to recover from the pension fund any tax charged as a result of inadvertently exceeding the MPAA.

1.4 This briefing proposes how those safeguards could be realised.

2 Safeguard 1 – keeping the level of the MPAA under review

2.1 To keep the MPAA at the reduced level of £4,000 in real terms, we strongly recommend that it is uprated each year. To do so, it could be uprated with other limits that are reviewed each

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year by reference to the Consumer Prices Index.[1] We therefore suggest the following amendment to clause 16, at page 18, line 34, at end insert:

> '(4A) After section 227G there shall be inserted:
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> "227H(1). If the consumer prices index for the September before the start of a tax year is higher than it was for the previous September, the amounts specified in sections 227ZA(1)(b), 227B(1)(b) and (2), and 227D(4) Steps 4 and 5 shall be indexed in the same way as adjusted net income as set out in section 57(4) Income Tax Act 2007.
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> 227H(2) Before the start of the tax year the Treasury must make an order replacing the amounts specified in the provisions listed in the sections referred to in subsection (1) above with the amounts which, as a result of applying the calculation specified in section 57(4) Income Tax Act 2007, are the amounts for the tax year."'

2.2 We understand that the Government is keen to dissuade 'tax-free cash recycling' which might mean that people seek to get further tax relief on money they have just taken out of a pension.

2.3 But with pensions freedom, an individual might decide to take money out of their pension (currently allowed at age 55) – for example, to pay off their mortgage or other debts. They might then decide to use their new-found surplus in disposable income to put money back into pensions to provide a nest egg for their old age when they eventually decide to reduce their hours or stop working.

2.4 The money purchase annual allowance of £10,000 is very unlikely to catch out too many people who might do this. But reducing it to £4,000 from April 2017 – equating to savings of £333 a month – is much more likely to cause problems for these people; especially if thinking about it in terms of someone choosing to save money they might have previously been paying on a mortgage. This is even easier to see as being a problem if we consider that the net of basic rate tax contribution – the amount the individual pays – would be £3,200, ie £266 per month. Such a monthly sum could well be half the person's previous mortgage repayments and therefore an easy sum to find for topping up their pensions.

2.5 While the consultation response document gives a welcome commitment to keeping the MPAA under review, it is concerning that there is no explicit commitment, which there ought to be, for the exact terms of such review. We are simply told that it 'will be kept under regular review, as are all aspects of the tax system'.[2] Given that the Office of Tax Simplification's 'List of tax thresholds'[3] shows that there are many such monetary limits in

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[1] Section 57 of the Income Tax Act 2007

[2] See response document, para 2.8
https://www.gov.uk/government/consultations/reducing-the-money-purchase-annual-allowance

[3] See https://www.gov.uk/government/publications/list-of-tax-thresholds

the tax system that have been far from regularly reviewed, we would have preferred a clear commitment to a review at least every three years. This is particularly concerning given that pensions freedom is still in its infancy and it may still be too early to predict its impact on savings patterns.

2.6 What we propose above is annual uprating to ensure that the limit as least holds its value in real terms, but would nevertheless suggest that it is subject to future triennial reviews given that it is too soon to say what impact other measures such as pensions freedom and the Lifetime ISA will have on short, medium and longer term savings patterns.

3 Safeguard 2 – recovering an MPAA tax charge from the pension fund

3.1 If a tax charge arises as a result of exceeding the MPAA, we believe it should be made possible for this to be paid out of the pension fund. Otherwise, those of limited means might not be able to pay and could find themselves in financial hardship. We therefore suggest the following amendment to clause 16, at page 18, after line 34,[1] insert:

> '(4B) In section 237B (liability of scheme administrator), insert new subsection 1A as follows–
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> "(1A) This section also applies if–
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> (a) an alternative chargeable amount as defined in section 227ZA arises which results in a tax liability of any amount for the individual, and
> (b) the individual elects to the Commissioners for Revenue and Customs by 31 January next following the end of the tax year in which the tax charge arises to transfer liability to the scheme administrator."'

3.2 Presently it is only permitted for the tax liability to be transferred to the pension fund where the standard annual allowance applies and the tax charge is at least £2,000.[2] Extending this to allow those who have exceed the MPAA to opt for the same treatment would protect those who unwittingly trigger a tax charge but lack the means to pay it. This might be because, for example, they have directed all their surplus income to pension savings, or that their circumstances have changed between making the payment and finding out about the tax charge.

3.3 While we acknowledge that the saver in this situation will have already withdrawn pension funds previously and therefore should be eligible to withdraw more pensions money to pay

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[1] Of the Bill, as introduced
https://www.publications.parliament.uk/pa/bills/cbill/2016-2017/0156/17156.pdf

[2] Para 2.10 of the consultation document: https://www.gov.uk/government/consultations/reducing-the-money-purchase-annual-allowance

the tax due, 75% of such a withdrawal would in itself be taxable income. This could therefore create a near-double tax charge on someone who has likely made a mistake, which would seem inequitable. Fairer rectification of that mistake would therefore be to transfer liability to the pension fund, at the taxpayer's behest.

3.4 If the taxpayer has more than one pension fund, the above suggested provision should be broad enough to allow them to elect from which scheme the charge is to be paid.

4 About LITRG

4.1 The LITRG is an initiative of the Chartered Institute of Taxation (CIOT) to give a voice to the unrepresented. Since 1998 LITRG has been working to improve the policy and processes of the tax, tax credits and associated welfare systems for the benefit of those on low incomes. Everything we do is aimed at improving the tax and benefits experience of low income workers, pensioners, migrants, students, disabled people and carers.

4.2 LITRG works extensively with HM Revenue &Customs (HMRC) and other government departments, commenting on proposals and putting forward our own ideas for improving the system. Too often the tax and related welfare laws and administrative systems are not designed with the low-income user in mind and this often makes life difficult for those we try to help.

4.3 The CIOT is a charity and the leading professional body in the United Kingdom concerned solely with taxation. The CIOT's primary purpose is to promote education and study of the administration and practice of taxation. One of the key aims is to achieve a better, more efficient, tax system for all affected by it – taxpayers, advisers and the authorities.

LITRG
13 October 2017