

USS

The annual allowance and the effect of the taper

At a glance information

- Should your benefit accrual over the year exceed £40,000, then you will be taxed on the excess at your highest marginal rate unless you have unused excess from the three prior years.
- Transitional arrangements are in place for the 2015/16 year to align scheme practice and tax years (this is explained in greater detail in the tax section of uss.co.uk).
- From April 2016, members with taxable income in excess of £110,000 will need to consider the application of the annual allowance and the effect of the taper.
- **You should read further if you expect your taxable income from all sources in the 2016/17 tax year to exceed or be near to £110,000.**

The annual allowance and the effect of the taper

What is the annual allowance?

Members are restricted in the amount of tax preferential pension benefits that can be accrued in a tax year by the annual allowance (AA). The table below shows that there isn't a single AA and your income or indeed the way in which you draw benefits can affect the amount you can accrue in a tax year.

Annual allowance	Amount	Application
Standard annual allowance	£40,000 per annum	Accrual in excess of £40,000 is taxed at your highest marginal rate.
Tapered annual allowance (effective from 6 April 2016)	£40,000 per annum reducing to £10,000 per annum	The taper applies for "adjusted income" over £150,000 per annum.
Money Purchase annual allowance (effective from 6 April 2015)	£10,000 per annum	Applies when a member makes specific withdrawals from a defined contribution arrangement.

How the AA taper will apply

The level of annual allowance is tapered, which means the amount of pension saving which attracts tax relief lowers as your income increases.

You could have a lower annual allowance if your taxable income, which HMRC refers to as your 'threshold income', is over £110,000 during the tax year - you should include property and investment income, for example. If that is the case, a further test is triggered to calculate your 'adjusted income.'

The definitions of these two key income measures are:

Threshold income	Adjusted income
<p>Broadly this is taxable income from all sources plus:</p> <ul style="list-style-type: none"> Any income sacrificed under a salary sacrifice arrangement entered into on or after 9 July 2015¹ minus; Pension contributions paid from taxed earnings² 	<p>Broadly this is threshold income, plus:</p> <ul style="list-style-type: none"> The 'value' of your employer contribution to any defined benefit arrangement, plus any employer contributions to a defined contribution arrangement.

If your adjusted income exceeds £150,000 then the annual allowance reduces by £1 for every £2 of income until this drops to £10,000.

Adjusted income	Annual allowance
£210,000	£10,000
£200,000	£15,000
£190,000	£20,000
£180,000	£25,000
£170,000	£30,000
£160,000	£35,000
£150,000	£40,000

¹ HMRC have yet to define the precise meaning of this. If a member had an existing salary sacrifice arrangement that reduced taxable income from £120,000 to £100,000, the working assumption is that the £100,000 is relevant for threshold income.

² For example you might pay contributions to a personal pension outside USS that uses a "relief at source" mechanism.

A particular difficulty in planning your pension arrangements, is that you may be unlikely to know your threshold income and indeed your adjusted income until the end of the tax year; which is too late to make arrangements for that year. You will therefore need to make a best estimate of your taxable income when considering these matters.

You are also likely to require the trustee company to provide you with information on your adjusted income as the 'value' of your employer contribution is not simply the amount paid to the scheme.

If my taxable income exceeds £110,000 how will I know whether the taper will apply?

The answer to this question is that you will not know for sure whether the taper will apply, or what the quantum of any reduction to the AA will be until the end of the tax year when an accurate calculation can be undertaken.

You can however estimate the figures with a view of your taxable income for the year and assistance from the trustee company to estimate the adjusted income figure. For the purpose of this mini factsheet we have estimated the adjusted income figure for illustration. A number of simplifying assumptions are made, but crucially we have assumed that your salary for USS purposes represents the only income you receive.

To explain what is happening in the illustrations below, the salaries are over £110,000 (threshold income) and therefore the test for the taper is triggered. That means that there is a calculation of adjusted income required i.e. your employer's contribution to your USS pension benefits must be added to the threshold income and that leads to the adjusted income figure. The AA is tapered where adjusted income exceeds £150,000.

As you can see from *Example 1* it is not the case that you will always have a tapered AA where you have exceeded threshold income definition. Numbers are rounded and the indicative tax charge is an illustration only.

Further information

USS is unable to accurately calculate the tapered annual allowance as the final calculations can only be undertaken accurately by the member after the end of the tax year when all relevant earnings are known.

Your pensions contact at your institution will be able to provide you with further assistance in relation to your pension benefits and USS can assist with estimated figures should you require them but specialist independent advice may be required. HMRC guidance for pension scheme trustees and providers is expected later in 2016.

	Example 1	Example 2	Example 3
USS salary	£120,000	£140,000	£180,000
Adjusted income	£140,000	£163,000	£210,000
Annual allowance	£40,000	£33,500	£10,000
Indicative tax charge	£nil	£1,000	£16,000

This publication is for general guidance only. It is not a legal document and does not explain all situations or eventualities. USS is governed by a trust deed and rules and if there is any difference between this publication and the trust deed and rules the latter prevail.

Every effort has been made to present accurate information at the date of publication and members are advised to check with their employer contact for latest information regarding the scheme, and any changes that may have occurred to its rules and benefits.