

**16 November 2017****Agenda Item: 9****REPORT OF THE SERVICE DIRECTOR – CUSTOMERS AND HUMAN  
RESOURCES****LOCAL GOVERNMENT PENSION SCHEME – ANNUAL ALLOWANCE –  
EXTENSION OF SCHEME PAYS TO INCLUDE VOLUNTARY FUNCTION.****Purpose of the Report**

1. To seek agreement from the Pensions Committee, in its role as Administering Authority of the Nottinghamshire Pension Fund, to extend “Scheme Pays’ to include Voluntary function for members of the Local Government Pension Scheme who breach HMRC’s annual allowance limit on pension savings growth in a financial year, and for agreement to the circumstances for accepting such applications.

**Information and Advice****Background**

2. The annual allowance is the annual limit on pension savings that can be made in each financial year which will receive tax relief. If the value of pension benefits grows by more than this allowance then the excess amount may become subject to a tax charge.
3. The 2016/17 standard annual allowance was set at £40,000, and remains at that rate for 2017/18.
4. However in the tax year 2016-2017, 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. This means for some individuals their annual allowance is reduced to £10,000.
5. Nottinghamshire Pension Fund has a statutory duty to write to scheme members who breach the annual allowance by 6 October in the tax year following the year in which the allowance was breached.
6. ‘Scheme Pays’ is a mechanism by which an individual can request that their annual allowance tax charge is met by the Pension Fund, in return for the member accepting an equivalent reduction to their pension benefit. “Mandatory Scheme Pays” has been available for many years. “Voluntary Scheme Pays” has now been identified by Local

Government Pensions Committee following legal advice as potentially available to LGPS members and this advice confirmed that administering authorities that are local authorities have vires to agree to a Voluntary Scheme Pays request.

7. The two types of 'Scheme Pays' are known as 'Mandatory' and 'Voluntary'. The differences are explained below -
8. **Annual Allowance - 'Mandatory Scheme Pays'**. 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.
9. **Annual Allowance – "Voluntary Scheme Pays"**. Where the scheme member's annual allowance tax charge is less than £2,000 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.
10. 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
11. Where the member's annual allowance has been reduced to £10,000, (s)he 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.
12. The Voluntary Scheme Pays option could be utilised to the benefit of Nottinghamshire Pension Fund members in such circumstances by enabling the tax charge to be paid by the Pension Fund and recovered through the payment of reduced pension benefits to the member. This could potentially impact on a number of scheme members. The extension of this provision would also potentially benefit the 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.
13. For clarity, if a member exceeds the annual allowance by virtue of savings across multiple pension schemes, without exceeding the annual allowance in any one scheme and a tax charge were to arise, it would not be appropriate for the Nottinghamshire Pension Fund to offer the Voluntary Scheme Pays option.
14. The Secretary of State for Communities and Local Government in conjunction with consultation by Government Actuaries Department (GAD) has issued guidance on the

calculation of the reduction in a members pension benefits following a Scheme Pays election. This ensures that the scheme pays offset is cost neutral to the scheme.

15. The understanding of the Nottinghamshire LGPS Administering Authority is that other East Midland LGPS Administering Authorities have adopted “Voluntary Scheme Pays”. This includes Leicestershire and Derbyshire Funds. The Greater Manchester Pension Fund, one of the largest, has also adopted the voluntary scheme. Nottinghamshire Fire and Rescue Service have adopted the scheme as has the Teachers’ Pension Scheme. Therefore, a decision to extend “Voluntary Scheme Pays” would align the Nottinghamshire LGPS Fund with other funds within local government and across the public sector.
16. Officers considering the application of Voluntary Scheme Pays would normally allow a member to use “Voluntary Scheme Pays” where the member has been subject to a tapered annual allowance and in exceptional circumstances allow this facility to be used where the member’s tax charge is below £2000.
17. The attached appendix is a factsheet produced by the LGPS regarding annual allowance which supports the extension of the Scheme Pays provision to include Voluntary.

## **Statutory and Policy Implications**

18. This report has been compiled after consideration of implications in respect of crime and disorder, data protection and information governance, finance, human resources, human rights, the NHS Constitution (public heather services), the public sector equality duty, safeguarding of children and adults at risk, service users, smarter working, sustainability and the environment and where such implications are material they are described below. Appropriate consultation has been undertaken and advice sought on these issues as required.

## **Data Protection and Information Governance Implications**

19. The data in this report and the appendix cannot be attributed to individual LGPS members. A number of Scheme members are potentially impacted across a number of Scheme Employers within the Nottinghamshire Pension Fund.

## **Recommendation**

20. That the Pensions Committee, in its role as the Administering Authority of the Nottinghamshire Pension Fund considers extending ‘Scheme Pays’ function to include Voluntary Scheme Pays as set out in paragraph 16.

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### **Constitutional Comments (SLB 6/11/17)**

Nottinghamshire Pensions Committee is the appropriate body to consider the content of this report.

### **Financial Comments (NS 28/7/17)**

The report indicates that the incidence of the introduction of the voluntary scheme is likely to be low. The actuarial reduction to the pension benefit ensures this is only an issue of cash flow management and ensures the Pension Fund is no worse off as a consequence of introducing this scheme.

### **Background Papers**

None

### **Electoral Division(s) and Member(s) Affected**

All