Lifetime allowance pension trap for NHS Dentists

Jon Drysdale explains the latest in pension regulations

**Pension capital value:**
- **Tax free lump sum:** £62,500 x 20 = £1,250,000
- **Total capital value:** £187,500
- **LTA (from 2014/15):** £1,250,000
- **Excess:** £187,500

The LTA charge payable to HMRC is 25 per cent of £187,500 = £46,875. This is recovered by reducing the annual pension amount by the charge, divided by a standard factor of 20. In this case the reduction is £2,344 pa. Income tax applies to the full pension in the normal way.

**Deemed value**

How is my NHS pension valued? The final pension income is multiplied by 20 in order to arrive at a ‘deemed value’. For example gross pension income of £62,500 equates to a value of £1.25m. However, as most dentists recently opted to remain on the ‘1095’ NHS pension scheme the automatic tax free cash of three times the pension income must also be accounted for. In this example an additional £187,500 has to be added to the valuation (£x £62,500) in respect of tax free cash, giving a total value of £1,437,500.

What are the penalties for exceeding the LTA? For the above example the excess charge is calculated as follows:

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\text{Excess charge} = \left( \frac{\text{Deemed value}}{20} - \text{LTA} \right) \times 0.25
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= \left( \frac{\£1,437,500}{20} - \£1,250,000 \right) \times 0.25 = \£2,344
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\text{Income tax applies to the full pension in the normal way.}
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**Careful planning is required here especially if personal pension funds are involved**

Luminaries pension allowances

Is it only the NHS pension that counts towards the limit? No, any personal pension funds (actual values) are added to the capital value of the NHS pension and the appropriate 25 per cent charge is applied to income and 55 per cent to lump sum benefits. Pension already in payment is included in the valuation calculations. This is to prevent tax charge avoidance through a phased drawing of benefits.

**Transitional protection**

How can the charge be avoided? We expect ‘transitional protection’ arrangements to be offered prior to the April 2014 deadline. This is in line with the transitional arrangements for previous changes to the LTA. However, to be effective it is likely the member will have to stop contributions to the pension scheme and forgo further benefit accrual. Those who previously applied for HMRC ‘protection’ may have already lost this, especially if they continued to make pension contributions.

For those who are under the current £1.5m limit but are likely to breach the new £1.25m limit, it may be advisable to start taking all pension benefits by April 2014. However, careful planning is required here especially if personal pension funds are involved.

For some it may be advantageous to remain within the pension scheme and suffer the charge. It will be important to assess your individual circumstances before taking this decision.

**Money Matters**

**About the author**

Jon Drysdale is a director of PFM Dental and an independent financial adviser. PFM Dental has offered specialist financial planning advice to dental practitioners since 1990 and are experts on the NHS pension as well as providing a specialist accountancy service for dentists. Visit www.pfmdental.co.uk for further information.