The Treasury
Yn Tashtey

INCOME TAX DIVISION
Government Office, Douglas
Isle of Man, British Isles
IM1 3TX

Assessor
M Couch

Telephone: (01624) 685400
Fax: (01624) 685351
E-mail: incometax@itd.treasury.gov.im
Website: www.gov.im/incometax

PRACTICE NOTE

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TAXATION OF MANX PENSION SCHEMES REFORM – TRANSITIONAL ISSUES

Introduction

The Income Tax (Pensions) Bill 2007 recently introduced into the Branches of Tynwald, will make major changes to the taxation of pensions on the Island. New provisions are scheduled to take effect from 6 April 2008.

Further detailed guidance will be issued once the Bill receives Royal Assent. In the meantime, this Practice Note deals with some transitional issues.

In this Practice Note reference is made to the following:

- Income Tax (Pensions) Bill 2007 ('the Bill')
- Income Tax (Retirement Benefit Schemes) Act 1978 ('the 1978 Act')
- Part 1 Income Tax Act 1989 ('the 1989 Act')
- 'Relevant Earnings' will be defined in both the 1978 and 1989 Acts (see clause 13(5) and 16(4) in the Bill).

Annual Allowance

The new legislation will repeal the percentage based approach to contributions and rules dealing with the carry forward of unutilised relief and the carry back of contributions. Instead, the concept of an annual allowance will be introduced. The Bill proposes that the annual allowance will start at £300,000. Tax relief will be available on contributions, into all approved schemes, up to the annual allowance providing there are sufficient relevant earnings in the tax year. If relevant earnings are lower than the annual allowance, tax relief will be limited to 100% of those earnings.

The Bill will also introduce a new minimum allowance, available to those people with little or no relevant earnings. As this is not a transitional issue more information will be provided in the detailed guide.

Pension contributions paid in the tax year ended 5 April 2008 will be subject to the current pension rules. Pension contributions made on or after 6 April 2008 will be subject to the new legislation (i.e. the annual allowance of £300,000, subject to the availability of relevant earnings).

Example

- In 2007/2008 a 35 year old scheme member wants to contribute £75,000 to an approved personal pension scheme, his relevant earnings are £35,000. He has no unused relief available from earlier years. The 1989 Act will only permit the member to contribute £6,125 (i.e. 17½% of his relevant earnings), no further contributions are allowed.

- During 2008/2009 the same scheme member wants to contribute £75,000 to an approved personal pension scheme, his relevant earnings remain £35,000. The scheme member will be able make the full contribution (*) and he can claim a deduction through his assessment equal to his salary, i.e. £35,000. No tax relief will be available on the contribution above £35,000.

  (*) provided the aggregate of all contributions by the member, his employer, etc. to all approved schemes does not exceed the annual allowance.

Carry Forward Relief and Carry Back of Contributions

The 1989 Act currently allows a member to claim unused relief for a period up to six years and, subject to a prescribed time limit, to elect for a contribution to be treated as if the payment was made in an earlier year of assessment. The Bill will repeal provisions in section 15 and 16 of the 1989 Act, limiting future contributions based on relevant earnings and the new annual allowance.

Recognising the fact that contributions made during 2007/2008 may have been determined based on the existing carry forward and carry back rules, the Assessor will allow premiums paid in 2007/2008 to be treated as paid in an earlier year, provided the election is made by 5 July 2008 (the latest date previously available under section 15 of the 1989 Act).

Following the previous example, if the scheme member had sufficient unused relief in 2006/2007 to cover the £75,000 contribution, he could elect (before 5 July 2008) to treat the 2007/2008 contribution as being paid and deductible in 2006/2007.

For the avoidance of doubt:

- The repeal of sections 15 and 16 only affects personal pension schemes approved under Part 1 of the 1989 Act. The repeal does not impact on contributions to occupational schemes approved under the 1978 Act; and
- The ability to carry back contributions does not include contributions paid during 2008/2009. Contributions made after 6 April 2008 will be considered in line with the new annual allowance approach.

Triviality Limit

On 19 June 2007 Tynwald approved a Treasury concession (Government Circular 21/07) allowing pension trustees to pay a trivial commutation lump sum up to a limit of £16,000 in cases where the member wished to 'cash-in' a pension fund or where the member was unable to acquire a suitable pension (e.g. annuity) due to the small fund available.

With effect from 6 April 2008 the trivial commutation lump sum limit shall be increased to £16,500 in line with the amount set by HMRC.

It has been proposed that the concession is to be replaced by Tynwald regulations as soon as practicable after the Bill has been passed.

M Couch

Assessor of Income Tax

This Practice Note is intended only as a general guide and must be read in conjunction with the appropriate legislation. It does not have any binding force and does not affect a person's right of appeal on points concerning their own liability to income tax.

Comments and suggestions for improvements of issued Practice Notes and suggestions for future Practice Notes are always welcome.