Local Government Pension Scheme

Dyfed Pension Fund

Voluntary Scheme Pays Policy

March 2025

Contents

Interpretation

"Fund"	Dyfed Pension Fund
"Administering Authority"	Carmarthenshire County Council

Summary

Scheme Pays is a process which may allow part or all of a member's annual allowance tax charge to be paid by the Pension Fund, in exchange for a reduction in their pension benefits. There are two types of Scheme Pays. They are called Mandatory and Voluntary, and this document covers both.

Introduction

The Annual Allowance was introduced in 2006 and is the amount that the overall value of a member's pension benefits can increase by in a Pension Input Period (currently aligned to the tax year) before potentially incurring an additional tax charge. In certain cases, members have an automatic entitlement under Section 237B of the Finance Act 2004 to ask the Fund to pay the tax charge on their behalf, and in return, have a corresponding reduction to their benefits when they leave the scheme. The reduction is applied to the member's pension account in the relevant tax year and will be increased with inflation until the benefits are paid. This is known as Mandatory Scheme Pays.

In other cases, members may ask the Fund to pay the tax charge, but there is no entitlement, and the Fund does not have to agree. The Administering Authority will consider each case on its merits and where the Fund does agree to pay the tax charge, the member's benefits will be reduced accordingly. The reduction is applied to the member's pension account in the relevant tax year and will be increased with inflation until the benefits are paid. This is known as Voluntary Scheme Pays. Members cannot use Scheme Pays once they are in receipt of their benefits, although it can still be used where the member has taken flexible retirement and is still building up further benefits in the Fund which are then subject to an Annual Allowance tax charge. This is the Voluntary Scheme Pays Policy of the Pension Fund, which is managed by the Administering Authority. The Policy details the circumstances in which an election for Voluntary Scheme Pays will be accepted by the Pension Fund. This Voluntary Scheme Pays Policy is established to provide clarity for Fund members who may wish to make an election for Voluntary Scheme Pays, and to ensure consistency of approach across the Fund. The Pensions Manager is responsible for ensuring that this policy is followed.

Aims and Objectives

In relation to the administration and communications of the Fund, the Administering Authority has a number of objectives including to:

- Provide a high quality, professional, proactive, timely and customer focussed administration service to the Fund's stakeholders.
- Ensure the correct benefits are paid to, and the correct income collected from, the correct people at the correct time.
- Promote the Scheme as a valuable benefit and provide sufficient information so members can make informed decisions about their benefits.
- Communicate in a clear, concise manner.

Having a policy setting out the circumstances in which an application for Voluntary Scheme Pays will be accepted supports the Administering Authority in achieving these objectives.

Background

This is a brief outline of the Annual Allowance and it is the member's responsibility to seek advice on the specific requirements. Further information is available on the HMRC website: https://www.gov.uk/tax-on-your-private-pension/annual-allowance

The concept of the Annual Allowance was introduced from April 2006 under the Finance Act 2004 and is the amount that the overall value of a member’s pension benefits can increase over a Pension Input Period (currently aligned to the tax year) before tax is due. The current Standard Annual Allowance for the majority of people is £60,000, (this increased from £40,000 to £60,000 on 6 April 2023) and if the increase in the value of a member’s pension benefits (their Pension Input Amount) in the relevant tax year exceeds that amount a tax charge may be due. Scheme members can carry forward any unused allowance from the previous three years to offset a potential tax charge. The Pension Input Amount is the amount that the overall value of a member’s benefits has increased between the start and end of the tax year. Higher earners and those with substantial taxable income from other sources (including pensions in payment) could be subject to the Tapered Annual Allowance, giving them an Annual Allowance lower than the Standard Annual Allowance and which could be as low as £10,000 (this was previously £4,000 for tax years April 2020 to March 2023 and £10,000 for tax years between April 2016 to March 2020). This affects anyone who meets both of the following criteria:

- Threshold Income is £200,000 or more (£110,000 for tax years between April 2016 to March 2020). Threshold Income is taxable income after employee pension contributions are deducted, and includes taxable income from all sources, not just salary.
- Adjusted Income exceeds £260,000 (£240,000 for tax years 2020 to 2023 and £150,000 for tax years between April 2016 to March 2020). Adjusted Income is Threshold Income plus Pension Input Amount.

If someone meets both criteria, their individual Annual Allowance is reduced by £1 for every £2 that their Adjusted Income exceeds £260,000. However, the member's Tapered Annual Allowance cannot be reduced below £10,000. Further information is available on the HMRC website: https://www.gov.uk/guidance/pension-schemes-work-out-your-tapered-annual-allowance]

Members who have previously 'flexibly accessed' benefits from a separate defined contribution pension plan will be subject to the Money Purchase Annual Allowance, currently £10,000 (this was previously £4,000 for tax years April 2017 to March 2023 and £10,000 for tax years between April 2015 to March 2017), and must inform the Pension Fund if this applies as this reduces the Annual Allowance used to test the LGPS benefits. Further information can be found in the section headed 'check if you've gone above the money purchase annual allowance' on the HMRC website: https://www.gov.uk/guidance/work-out-your-allowances-if-youve-flexibly-accessed-your-pension

Tax arising from exceeding the Annual Allowance is charged at the member's marginal rate of income tax (20%, 40% or 45% in whole or in part depending on total taxable earnings) on the amount of pension input that exceeds the member's Annual Allowance, taking account of any carry forward of unused allowance from previous years. It is the member's responsibility to determine the rate of tax applied.

Mandatory Scheme Pays

Where a member has a tax charge as a result of breaching the Annual Allowance, they have a right to Mandatory Scheme Pays from the Pension Fund when ALL of the following criteria are met:

- The member's Annual Allowance tax charge exceeds £2,000, and
- The member has a Pension Input Amount within the LGPS in England and Wales exceeding the standard Annual Allowance (currently £60,000), and
- An irrevocable election for Mandatory Scheme Pays is made by 31st July in the year following that in which the tax charge arose (i.e. for a tax charge arising from

the 2022/2023 year the Mandatory Scheme Pays election must be made by 31st July 2024) or before they retire, if earlier, and

- The member's full retirement benefits from the Fund are not yet in payment.

Where a member does meet all the above criteria, the Pension Fund must pay the tax to HMRC on the member's behalf when requested and must notify the member of the resulting reduction to their benefits. The Fund is not allowed to levy an administration charge for Mandatory Scheme Pays elections. Note that a member does not need to ask the Fund to pay the full tax charge – the member can request that a lower amount is covered by Mandatory Scheme Pays and would have to make their own arrangements to pay the remaining tax charge to HMRC. Members should note that their pension cannot be reduced below the level of their Guaranteed Minimum Pension (GMP), so the Fund may not be able to pay the full tax charge if the corresponding reduction to benefits would reduce the pension below GMP.

For Mandatory Scheme Pays, the member must indicate to HMRC that they will be using Mandatory Scheme Pays on their self-assessment tax return by 31 January in the year following that in which the tax charge arose, but the election to the Fund does not have to be made until 31 July, six months later, and the Fund then has until the following 14 February to pay the tax. A different deadline for Mandatory Scheme Pays may apply where the Fund notifies a member of a change to an earlier Pension Input Period. Where this applies the Fund will advise the scheme member of the revised deadline.

Voluntary Scheme Pays

The list below shows some potential situations in which a member may have incurred a tax charge but does not have an entitlement to Mandatory Scheme Pays. In these situations the member can ask their scheme to allow a Voluntary Scheme Pays election, but the scheme does not have to agree. This list is not intended to be exhaustive.

- The member is subject to the Tapered Annual Allowance or the Money Purchase Annual Allowance, and their Pension Input Amount in the LGPS exceeds their Tapered/Money Purchase Annual Allowance but does not exceed the Standard Annual Allowance.

- The member is subject to the Tapered Annual Allowance or the Money Purchase Annual Allowance, and their Pension Input Amount in the LGPS exceeds both the Tapered/Money Purchase Annual Allowance and the Standard Annual Allowance – there is a right to Mandatory Scheme Pays in respect of the input above the Standard Annual Allowance, but not for the input between the Tapered/Money Purchase Annual Allowance and the Standard Annual Allowance.

- The member met all the other criteria for a Mandatory Scheme Pays election, but did not make the election by the 31st July deadline (or any revised deadline that applies where a change to an earlier Pension Input Period has been notified).
- The member has not exceeded the Annual Allowance based on their pension benefits in the LGPS in England and Wales, but in aggregate across all pension arrangements they have exceeded the Annual Allowance and the member's total tax charge when taking input from other arrangements into account is more than £2,000.
- The member has a Mandatory Scheme Pays right in respect of pension input in the LGPS in England and Wales, but also has a tax charge relating to input in a separate pension arrangement and wants to use Voluntary Scheme Pays from the Fund to cover this as well.
- The member's full retirement benefits are in payment.

There is no time limit set in the legislation for an election for Voluntary Scheme Pays (if permitted), but members should note that if the tax is not paid by 31st January in the year following the year in which the tax charge arises (i.e. 31st January 2024 for a tax charge arising in the 2022/23 year) interest and late payment penalties will be due. Interest and late payment penalties do not apply for tax charges that are settled by Mandatory Scheme Pays, assuming the member provides the appropriate notifications to HMRC via self-assessment or otherwise, because in this circumstance the member and the Administering Authority are jointly and severally liable for the payment of the tax charge, whereas the member remains solely liable for any tax due that is not covered by Mandatory Scheme Pays.

Tapered Annual Allowance Examples

- Member's Pension Input Amount is £80,000 and they are subject to a tapered annual allowance of £10,000. The tax charge will be £28,000 assuming they are a 40% taxpayer and have no carry-forward available. Mandatory Scheme Pays only applies to £8,000 of that tax charge (in respect of the input in excess of £60,000). The remaining £20,000 of the tax charge would need to be settled by the member directly with HMRC, unless a Voluntary Scheme Pays arrangement is agreed with the Fund.
- Member's pension input is £39,000 and they are subject to a tapered annual allowance of £10,000. Their tax charge will be £11,600 assuming they are a 40% taxpayer and have no carry-forward available. This does not qualify for Mandatory Scheme Pays as the pension input is less than the Standard Annual

Allowance of £60,000, so would need to be settled by the member directly with HMRC, unless a Voluntary Scheme Pays arrangement is agreed with the Fund.

It should be noted that it is the member's responsibility to notify the Fund if they are subject to a Tapered Annual Allowance and the amount of tax due. The Fund cannot calculate this as it does not have details of total taxable income.

Pension Fund Policy

The Fund will accept applications for Voluntary Scheme Pays in the following circumstances:

- A member is subject to the Tapered Annual Allowance or the Money Purchase Annual Allowance and has a tax charge of more than £2,000 relating to input in the Pension Fund, and the irrevocable election is received by 30th November following the end of the tax year in which the input arises (i.e. 30th November 2023 for input in the 2022/23 year).
- A member meets all the criteria for Mandatory Scheme Pays but was unable to meet the 31st July deadline due to an administrative error or omission by the Pension Fund (i.e. the member was not notified of their pension input in time for them to meet the deadline). In these circumstances the application for Voluntary Scheme Pays should be made within 2 months of the member receiving notification of their pension input.
- A member is notified of a change to an earlier Pension Input Period but does not meet the criteria for Mandatory Scheme Pays. In these circumstances the application for Voluntary Scheme Pays should be made within 2 months of the member receiving notification of their amended pension input.

The Fund will not accept applications for Voluntary Scheme Pays in the following circumstances:

- The member's tax charge relating to pension input in the LGPS in England & Wales is less than £2,000, but they have applied for Voluntary Scheme Pays because their total tax charge when taking input from other arrangements into account is more than £2,000.
- The member has a Mandatory Scheme Pays right in respect of pension input in the LGPS in England and Wales, but has also asked the Fund to pay a tax charge relating to input in a separate pension arrangement.
- A member did not meet the 31st July deadline for applying for Mandatory Scheme Pays (or any later deadline that may apply where a change to an earlier

Pension Input Period has been notified) and this failure to meet the deadline was not due to any administrative error or omission by the Pension Fund.

- All of a member’s retirement benefits have been put into payment.

A Voluntary Scheme Pays request in any other scenario will be considered on its merits. Following the acceptance of an election for Voluntary Scheme Pays, the member's benefits will be reduced by an amount corresponding to the tax charge paid by the Fund, using the guidance issued by the Government Actuary's Department.

Members approaching retirement

There are situations where a member may breach the annual allowance in the Pension Input Period in which they retire, even if they retire relatively near the start of the tax year. This could be, for example, where there has been an ill health enhancement (and the member did not meet the severe ill-health condition under s229(4) of the Finance Act 2004) or a large pay increase, bonus or service enhancement before or at retirement. If a member breaches the annual allowance in the tax year in which they receive their final retirement benefits, only mandatory scheme pays can be used if the election is made and processed before the benefits are put into payment (or "crystallised"). Otherwise members will have to pay the tax charge directly as the Fund will not accept a voluntary scheme pays election once benefits are in payment. Members in this situation may choose to pay the tax charge using any lump sum payable on retirement. Members retiring between April and October should also ensure that they establish whether there was any breach in the preceding Pension Input Period before their benefits are finalised, as they will be retiring before the deadline for a Pensions Savings Statement to be issued. Again, any scheme pays election in respect of the preceding Pension Input Period must be made before the benefits are crystallised. The Fund will issue an individual pension savings statement to those active members who become a pensioner member during the Pension Input Period and who have exceeded the standard annual allowance. This will be provided when the retirement benefits are notified rather than under the usual timescales. This gives the member the time to determine whether a Mandatory Scheme Pays option applies and/or whether they wish to make an election for Mandatory or Voluntary Scheme Pays. If the member wishes to use Scheme Pays they should contact the Pension Fund well before the retirement date so that the relevant reduction can be calculated and applied before the benefits are put into payment. It should be noted that it is the member’s responsibility to notify the Fund at this time if they are subject to a Tapered Annual Allowance and the amount of tax due. The Fund cannot calculate this as it does not have details of total taxable income.

Costs

All costs related to the operation and implementation of this Policy will be met directly by the Pension Fund. Paying the tax charge should be cost neutral for the Fund, as the Government Actuary's Department has issued guidance for calculating the reduction to the member's benefits which should ensure that the Fund does not lose out. However, the Fund will incur administration costs for the time taken in dealing with member requests and paying the tax due to HMRC. It has been considered whether to apply an administration charge to members wishing to use Voluntary Scheme Pays, but due to the low numbers expected to take up this option it has been decided not to levy a charge at this time. This will be reviewed should it transpire to be administratively onerous to operate this policy.

Approval, Review and Consultation

This Voluntary Scheme Pays Policy was approved by pensions committee in the March 2025. This Policy will be reviewed every 3 years subject to no legislative change.