Typically a SSAS is a money purchase scheme as defined in the Pension Schemes Act 1993 s188, but, like any other occupational pension scheme, it can be either money purchase or defined benefits (DB) and in some circumstances it can be advantageous to be DB, typically final salary.

health warning: What I write were are short broad brush descriptions, which, unavoidably, are dangerously simplified and cannot be relied on to apply in any particular circumstances.

definition of "SSAS"

I continue to use the usual although technically obsolete acronym "SSAS" (small self-administered scheme) to describe a "small scheme", as defined in in the Occupational Pension Schemes (Investment) Regulations 2005, SI 2005/3378, namely that:

(a) it is an occupational pension scheme;
(b) it has fewer than 12 members; and
(c) all its members are trustees of the scheme and either
  (i) the provisions of the scheme provide that all decisions which fall to be made by the trustees are made by the unanimous agreement of the trustees who are members of the scheme, or
  (ii) the scheme has a trustee who is independent for the purposes of section 23 of the Pensions Act 1995

  (with corresponding requirements for directors of a company which is the sole trustee of the scheme).

money purchase or DB

In a money purchase scheme the employer or the employee or both of them pay contributions to the scheme in order to create a fund for the employee, which accumulate with interest and other investment returns until the employee retires and uses the fund to provide a pension or a lump sum and pension. A DB scheme works the other way round. The employer awards a pension, usually a percentage that accrues for each year of pensionable service, and must then provide sufficient funds, estimated by an actuary, to enable the scheme to provide the pension (or pension and lump sum).

tax limits

The Finance Act 2004 (as amended) limits the amounts contributed to a pension scheme that benefit from tax relief. What the limits are depends whether the scheme is money purchase or DB. The basic rule for both types of scheme is that tax relief is available in each input period (financial year) on a member's "pension input amount" up to the lower of his or her UK taxable earnings and his or her annual allowance (AA), which is £40,000. Up to three year's unused AA can be carried forward.

A member's input amount in a money purchase scheme is the amount of contributions paid by or for the benefit of the member. (FA 2004 s233)

Contributions have nothing to do with a member's input amount in a DB scheme, because they could be low or nil if the scheme is in surplus or high if the scheme is in deficit. Instead the input amount is measured by the benefit and the increase in its value over the

Roderick Ramage
BSc(Econ) solicitor
authorised and regulated by the Solicitors' Regulation Authority number 231800
Copehale, Coppenhall, Stafford, ST18 9BW
01785-223030, roderick.ramage@law-office.co.uk, www.law-office.co.uk, meals.decimals.wizard

pension input period with an inflation adjustment using the CPI. The value of a member's benefits is not their actuarial value, but the amount of the pension multiplied by 16. That factor is statutory and applies to all DB schemes. (FA 2004 s234)

<u>example 1</u> - money purchase pension

(a) annual earnings £30,000; maximum tax allowable contribution £30,000.

(b) annual earnings £100,000; maximum tax allowable contribution £40,000.

<u>example 2</u> - DB conventional annual accrual of pension

Pension accrual rate 1/60th of final salary for each year of pensionable service, 10 years' service, annual earnings of £100,000 at start of pension input period and £105,000 at end.

(a) opening input amount: (10 x £100,000 ÷ 60) = £16,667 (accrued annual pension)

£16,667 x 16 = £266,672. (CPI adjustment ignored)

(b) closing input amount: (11 x £110,000 ÷ 60) = £20,167 (accrued annual pension)

£20,167 x 16 = £322,672

Increase (b) – (a) = £56,000, which is the input amount. The £16,000 excess over the AA is liable to an AA tax charge.

<u>example 3</u> - DB single pension award (instead of annual accrual)

Annual earnings at least £40,000, no pensionable service, pension award £10,000.

(a) opening input amount: £0.

(b) closing input amount: £10,000 x 16 = £160,000.

Increase (b) – (a) = £160,000, (£120,000 in excess of AA, but 3 x unused AA brought forward = £120,000.

DB contributions

Whereas the amount of contributions paid to a money purchase scheme is the pension input amount, in a DB scheme the contributions paid do not affect the pension input amount, but are the amount advised by the actuary to be necessary to fund the pension, and, depending on the assumptions used, might but will not necessarily exceed the pension input amount.

statutory funding obligation and s75 deficit

The employers of a "normal" DB schemes are subject to the scheme funding obligation in part 3 of the Pensions Act 2004 and the debt on the employer (deficit on, inter ala, the winding up of the scheme under the Pensions Act 1995, s75.

The employer of a DB SSAS is, by reg 17 of SI 2005/3377, exempt from the scheme funding obligation and, by reg 10 of SI 1996/3128, (but only if the scheme has only one member) from s75.

HMRC

Some commentators suggest that DB SSASs are a "loophole" to circumvent the AA restrictions on contributions and so are liable to more stringent examination than other schemes, to which a retort is that the so-called loophole is no more than a reflection of the inherent actuarial uncertainty of DB schemes.

END