### Pensions Update 131

23rd April 2002

Please pass a copy of this Update to everyone in your organisation who needs to see it. The category of schemes covered by this Update is shown below. Italicised terms are explained in the glossary at the end.

<table>
<thead>
<tr>
<th>Category:</th>
<th>Occupational Pension Schemes.</th>
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</thead>
<tbody>
<tr>
<td>Action:</td>
<td>To note the position on the tax treatment of pension contributions for part-time employees who are being given rights to retrospective membership of occupational pension schemes following House of Lords ruling in Preston &amp; Others v Wolverhampton Healthcare NHS Trust &amp; Others (The Preston Case).</td>
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<tr>
<td>Current Position:</td>
<td>There has been some evidence that the settlement by employers of claims by employees has been held up pending confirmation of the tax position.</td>
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<tr>
<td>Summary:</td>
<td>This Update provides confirmation of the tax position.</td>
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<td>Enquiries:</td>
<td>0115 974 1600 - Occupational pensions schemes Helpline.</td>
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**U 131: Part-time Employees**

**RIGHTS TO RETROSPECTIVE MEMBERSHIP OF OCCUPATIONAL PENSION SCHEMES FOLLOWING COURT RULINGS IN THE PRESTON CASE**

1. This Update is to confirm the tax position on pension contributions relating to part-time employees who are given backdated rights to membership of occupational pension schemes. The tax position was confirmed by the Economic Secretary to the Treasury in answer to a Parliamentary Question on 25 March.

**Background**

2. Mrs Preston was not allowed to join her employer's pension scheme as she worked part-time. However full-time employees were allowed to join the scheme. Consequently she took her case to the European Court of Justice who found that she had a right to retrospective membership. The UK courts were then asked to rule on the extent of the retrospective rights and also the time limits for claims.

3. The House of Lords found that an employee can claim retrospective rights back to 8 April 1976, or the date the employment started if later. A part-time employee may claim to an Employment Tribunal, where this constitutes sexual discrimination, in a period up to 6 months after leaving the employment concerned. The rulings also established that the employee is required to pay any compulsory employee's contributions that would have been due.
Redress

4. It is for employers to settle with their employees how they should meet any entitlement to retrospective rights. Such redress may be as a result of a ruling from an Employment Tribunal, or may be through an informal settlement.

Tax Treatment

5. The Economic Secretary to the Treasury, in answer to the Parliamentary Question referred to at 1 above, has confirmed that normal tax rules will apply. The following paragraphs explain the position.

Employer Contributions

6. Contributions from an employer to fund back service will be allowable for tax purposes in the normal way under section 592(4) of the *Taxes Act*.

Employee Contributions

7. Contributions made by the employee to the occupational pension scheme to catch up may be made as a single contribution, or as on-going contributions as described in paragraph 9 below. Tax relief under section 592(7) or section 594(1) of the *Taxes Act* will be available. The limit of such relief is 15% of remuneration paid in the tax year in which the contribution was made in relation to the specific employment concerned. There is no prescription by the Board of Inland Revenue to apply any higher limit for tax relief in these circumstances.

8. Scheme rules would normally preclude the payment of contributions by members which are in excess of the limit for tax relief (PN 4.4). But there will be no objection to an employee paying contributions in excess of the 15% limit in the circumstances described in this Update. Rules may therefore be amended accordingly. But tax relief will not be available on the excess over the 15% limit.

9. An employee cannot opt to carry back or have payments otherwise related back to earlier years, but the payment of contributions attributable to back years may, if agreed with the scheme trustees, be made by instalments over future years. This could be done to keep the amount paid in any one tax year within the 15% limit.

10. If an employee has left the employment concerned, but is to contribute to the former employer’s occupational pension scheme, such contributions may be made but no tax relief will be available. This will not affect the normal right of the employee to pay contributions of up to 15%, with tax relief, for any current employment.

Contracting Out

11. Where retrospective membership is to apply to a contracted out scheme, arrears of contracted out contributions would need to be paid. To the extent that tax relief is available on such contributions, for example on flat-rate payments of the employee’s share of minimum payments, tax relief may be given under the same rules as above.

Lump Sum Settlements

12. If employers and their employees agree on compensatory lump sum settlements outside of the pension scheme rather than additional membership rights under an occupational pension scheme, these lump sums will not be taxable as income of the employee under Schedule E. The employee may be liable to capital gains tax, but the usual normal annual exemption limits will apply. Questions relating to capital gains tax on such payments should be directed to the Tax Office.

13. Where redress within a pension scheme is made for an employee who has already taken benefits, for example in relation to later full-time service, it will not be acceptable for an additional retirement lump sum to be provided. However, if a transfer payment has been made and a further
enhancement of benefits now arises, it will be permissible to pay a second transfer payment as described in Update No 40.

**Personal Pension Schemes**

14. It is our understanding that the Court rulings relate only to occupational pension schemes. They do not therefore apply to a personal pension scheme, including a group personal pension scheme, to which the employer may have contributed.

**Further information**

15. If financial advisers receive enquiries from individuals, they may wish to consider referring them to the employer or former employer, the scheme trustees, OPAS, a staff association or Trade Union, or the local Citizen Advice Bureau as appropriate. The Inland Revenue can only explain the tax position as it affects all schemes. Our staff cannot discuss with employees how individual schemes are dealing with the issue. Employees therefore should not be encouraged to contact this Office.

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**Glossary**

**OPAS**: The Pensions Advisory Service (Helpline 0845 6012923).

**Personal pension scheme**: A scheme that has been approved by the Inland Revenue for tax purposes under Chapter IV of Part XIV of the Taxes Act. The term includes stakeholder pension schemes.

**PN**: Practice Notes IR 12 (2001).