The Telefónica UK Pension Plan
The Summer Budget pension tax changes

Overview of the new pension tax changes

- The Government has announced that pension tax allowances are to be further reduced.
- The changes take effect from 6 April 2016.
- The reduced pension tax allowances may affect more members of the Telefonica UK Pension Plan (the Plan).
- If you believe you may be affected by the reduction in the pension tax allowances, the remainder of this document provides more details on the changes.

What are the changes being introduced?
From 6 April 2016, Her Majesty's Revenue & Customs (HMRC) will further restrict tax relief on pension savings by:

- **Introducing a Tapered Annual Allowance for individuals who have Threshold Income of more than £110,0000 and Adjusted Income of more than £150,000 (see below for more detail on this)**: this is the maximum value of tax relieved pension contributions that can be made each tax year

- **Reducing the Lifetime Allowance to £1 million**: this is the total value of pension savings you can build up over your entire working lifetime before a tax penalty applies.

If your pension savings exceed the Annual Allowance or Lifetime Allowance then penal tax charges will apply.

This note sets out a summary of how these changes are expected to work.

The Annual Allowance

The '**Annual Allowance**' is the amount of your annual pension savings that can benefit from tax relief. The most that you can save tax-free towards all your pension arrangements is the lower of 100% of your earnings and the Annual Allowance.

What is my "pension input period"?

The pension input period (PIP) for the Plan is in line with the tax year. All pension contributions paid in the PIP for each tax year will be compared to the Annual Allowance.

Although the PIP for the Plan is already in line with the tax year, this has not been the case for all pension schemes. In order to introduce the changes to the Annual Allowance from 6 April 2016, the Government needed to align all PIPs with the tax year.

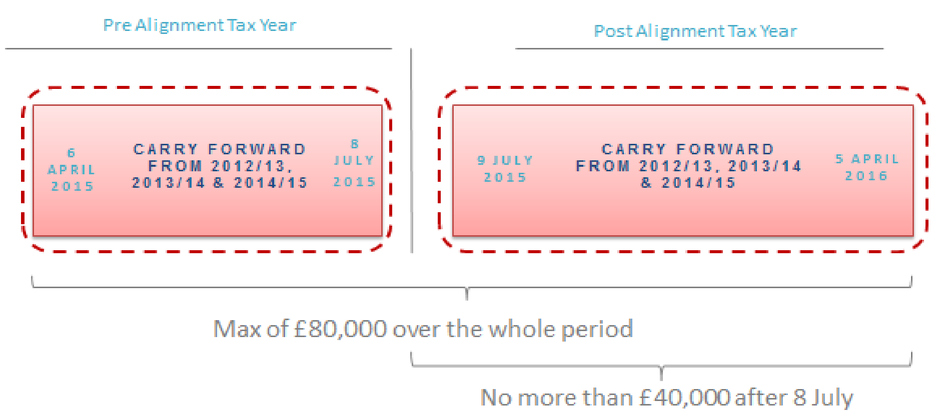
Special transitional rules will therefore apply for tax year 2015/16, which mean that the Plan will have two PIPs.

1. *Pre- alignment PIP – From 6 April 2015 to 8 July 2015*
2. *Post Alignment PIP – From 9 July 2015 to 5 April 2016*

How much is the Annual Allowance?

Pension contributions paid in the 2015/16 tax year will be tested against an Annual Allowance of £80,000. Where the £80,000 has not been used in the pre-alignment PIP (and you were a member of a registered pension scheme at any time between 6 April 2015 and 8 July 2015) it can be carried forward to the post-alignment PIP, subject to a maximum of £40,000. Your actual available tax relief for the 2015/16 tax year will depend on what pension contributions were paid prior to 9 July 2015.

- If £40,000 or less was paid up to and including 8 July 2015, your Annual Allowance from 9 July 2015 to 5 April 2016 will be £40,000.
- If more than £40,000 was paid up to and including 8 July 2015, your Annual Allowance from 9 July 2015 to 5 April 2016 will be the difference between what has been paid and £80,000.
- You can also 'carry forward' any unused Annual Allowance from the three previous tax years.



If you access you pension savings flexibly during the 2015/16 tax year transitional rules will apply and your Annual Allowance will be less than this.

Example 1 highlights how the Annual Allowance will operate for tax year 2015/16.

Example 1 – Tax year 2015/16

On 6 April 2015, Mike has a pensionable salary of £100,000. The Company currently contributes 21% of his pensionable salary to the Plan on a monthly basis.

Mike also pays additional monthly contributions of 9% of his pensionable salary to the Plan. Total contributions equate to £2,500 per month.

Pre-alignment PIP - 6 April 2015 to 8 July 2015	**Post-alignment PIP – 9 July 2015 to 5 April 2016**
3 months of £2,500 = £7,500	9 months of £2,500 = £22,500

Total contributions = £30,000

The Annual Allowance is £40,000 for the post-alignment PIP, which means Mike has scope to make additional tax relieved pension contributions of £17,500 plus any carry forward he has available for the 3 previous tax years.

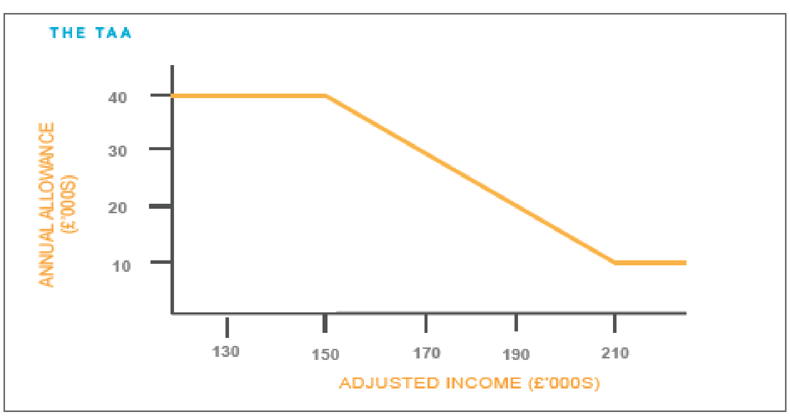
The Annual Allowance after April 2016

The Annual Allowance from 6 April will be £40,000; however, a Tapered Annual Allowance (TAA) will be introduced for Plan members with Threshold Income of more than £110,000 and Adjusted Income of more than £150,000. In broad terms:

"Threshold Income" *is total income subject to tax (earned and unearned) plus the value of pension contributions paid for new salary sacrifice arrangements established on or after 9 July 2015, less the value of any employee pension contributions.*

"Adjusted Income" *is total income subject to tax (earned and unearned), plus the value of employer and employee pension contributions.*

For individuals with both Threshold Income of more than £110,000 and Adjusted Income of more than £150,000, the Annual Allowance of £40,000 will be reduced by £1 for every £2 of Adjusted Income of more than £150,000 subject to a minimum of £10,000.



What happens if my pension savings exceed the Annual Allowance?

If your pension contributions exceed the Annual Allowance, they will be subject to an Annual Allowance tax charge. The tax rate applied to the excess amount will be equivalent to your marginal rate of income tax. The tax charge will be collected via your self-assessment tax return. In certain circumstances the Trustee of the Plan may allow the tax charge to be paid by making a reduction to your Plan benefits instead.

However, you may be able to offset the potential tax payable by carrying forward any unused Annual Allowance (effectively a "tax credit") from the previous three tax years based on a notional Annual Allowance of £50,000 for tax years prior to tax year 2014/15 and £40,000 from tax year 2014/15 onwards.

Because the Annual Allowance test is applied to all pension savings, any pension savings you make outside the Plan will also count towards the Annual Allowance.

Example 2 highlights how the Tapered Annual Allowance will operate for tax year 2016/17.

Example 2 – Tax year 2016/17

Sharon's Threshold Income for the tax year is £160,000 and the Company contributes 21% of her pensionable salary to the Plan on a monthly basis, which equate to £33,600 per annum. Sharon does not pay any employee contributions into the Plan.

Her Adjusted Income is therefore £193,600 (£160,000 + £33,600), which means she will be subject to the Tapered Annual Allowance. Her Tapered Annual Allowance will be £18,200 (£40,000 – (£193,600 - £150,000) / 2).

Sharon has the following unused Annual Allowances to carry forward from the previous three tax years:

Tax year 2015/16:	£10,000
Tax year 2014/15:	£15,000
Tax year 2013/14:	£20,000
Total =	£45,000

As Sharon does not make any employee contributions, the Company contribution made for tax year 2016/17 will use up £15,400 (£33,600 - £18,200) of her unused Annual Allowance for tax year 2013/14.

As Sharon has not used the remainder of her unused Annual Allowance for tax year 2013/14 of £4,600 (£20,000 - £15,400) it will be lost and she will have £25,000 (£15,000 for tax year 2014/15 plus £10,000 for tax year 2015/16) of unused Annual Allowances to carry forward for tax year 2017/18.

If you have already taken any pension benefits flexibly since 6 April 2015 (this could include flexible or flexi access drawdown or taken a lump sum in which was subject to income tax), your Annual Allowance will be reduced to £10,000, with transitional rules applicable to the 2015/16 tax year.

The Lifetime Allowance

The Lifetime Allowance is the maximum value of pension benefits that can be provided without triggering an extra tax charge.

The Lifetime Allowance is currently £1.25 million and will be reduced to £1 million from 6 April 2016. From 6 April 2018, it will increase in line with the Consumer Price Index (CPI).

How are pension benefits valued for Lifetime Allowance purposes?

Pension benefits will only be tested against the Lifetime Allowance when they are brought into payment or earlier death (please note a spouse's death in service pension will not count towards the Lifetime Allowance). The value placed on pension benefits for the purpose of testing against the Lifetime Allowance will differ depending on the type of pension arrangement you have:

- For defined benefit pension benefits, such as those with deferred benefits within Section 2 and 3 of the Plan, it is the actual retirement pension that you will receive, multiplied by a factor of 20, plus the face value of any defined benefit pension given up for tax free cash.

- For defined contribution benefits, such as those made to the Plan or any other defined contribution pension plans (including AVCs), it is the fund value at the time you decide to draw your pension benefits.

If you are a member of more than one pension arrangement, then the Lifetime Allowance test applies to the value of all your pension benefits from all pension arrangements, when any of these are brought into payment.

What happens if the value of my pension benefits is more than the Lifetime Allowance when I take them?

The excess value above the Lifetime Allowance will be subject to a:

- 55% tax charge if paid as a lump sum, or

- 25% tax charge if paid as a pension, with subsequent pension payments or income withdrawals being subject to income tax at your marginal rate.

The Lifetime Allowance charge will be met by the Plan by reducing your pension benefits.

What if the expected current value of my pension benefits is higher than £1 million after 6 April 2016?

To help to mitigate the impact of the penal tax charges applying to benefits in excess of the Lifetime Allowance, HMRC have confirmed that the following Lifetime Allowance protection options will be made available from 6 April 2016:

Fixed Protection 2016 - *Individuals will be provided with a Lifetime Allowance of £1.25 million. However, no further pension contributions can be made by or for them post 6 April 2016.*

Individual Protection 2016 – *If the value of pension your pension benefits at 5 April 2016 is more than £1 million, this will create your own personal Lifetime Allowance subject to a maximum of*

£1.25 million. Under this Lifetime Allowance protection option contributions can continue to be made by or for you post April 2016.

You will need to register for these protections before taking pension benefits.

How do I register for Lifetime Allowance protection?

Registration will need to be done on-line but this service will only be available from July 2016. For members whose benefits will come into payment on or after 6 April 2016 (but before July 2016), they will need to write to HMRC notifying them of their intention to apply for the protections.

Once you have successfully registered for Lifetime Allowance protection HMRC will provide you with a protection reference number which will you will need to pass on to the Plan administrator and the pension scheme administrators of any other pension arrangements you are a member of prior to taking pension benefits.

Where you should go if you need more information?

If you have any questions about this note please contact Gill Monk (gill.monk@telefonica.com)

If you are at all uncertain about making any decisions to do with your finances and benefits, please take advice. The Financial Conduct Authority website provides information in relation to finding a financial adviser at:

www.fca.org.uk/consumers/financial-services-products/investments/financial-advice/finding-an-adviser

You can also find guidance on using an adviser on the Money Advice Service's website.

www.moneyadviceservice.org.uk

Disclaimer

The information in this note is based on the guidance published on 8 July 2015 by HM Revenue & Customs, and is subject to change once the final legislation is enacted.

This note is intended for general information and illustrative purposes. It does not constitute investment or any other advice, and it is not intended to be a substitute for information and statements provided by the Telefónica *UK Pension Plan. It should not be relied on to make investment or other decisions.* Telefónica *give no warranty and accepts no responsibility for the accuracy of any information provided, or for your reliance on that information. Your benefits will be worked out in accordance with and subject to the governing trust deed and rules. Although every effort has been made to ensure that the information given in this note is accurate, none of the information given can give you legal rights to benefits that differ from those provided in the pension trust and rules.*

We recommend that you get independent financial advice before making any important decisions about your pensions arrangements.

Please note that neither the Telefonica UK Pension Plan Trustees, the employers, nor the Plan's administrator are able to provide you with financial advice and this information contained in this note and any other communication relating to the summer budget changes should not be treated as advice.

November 2015