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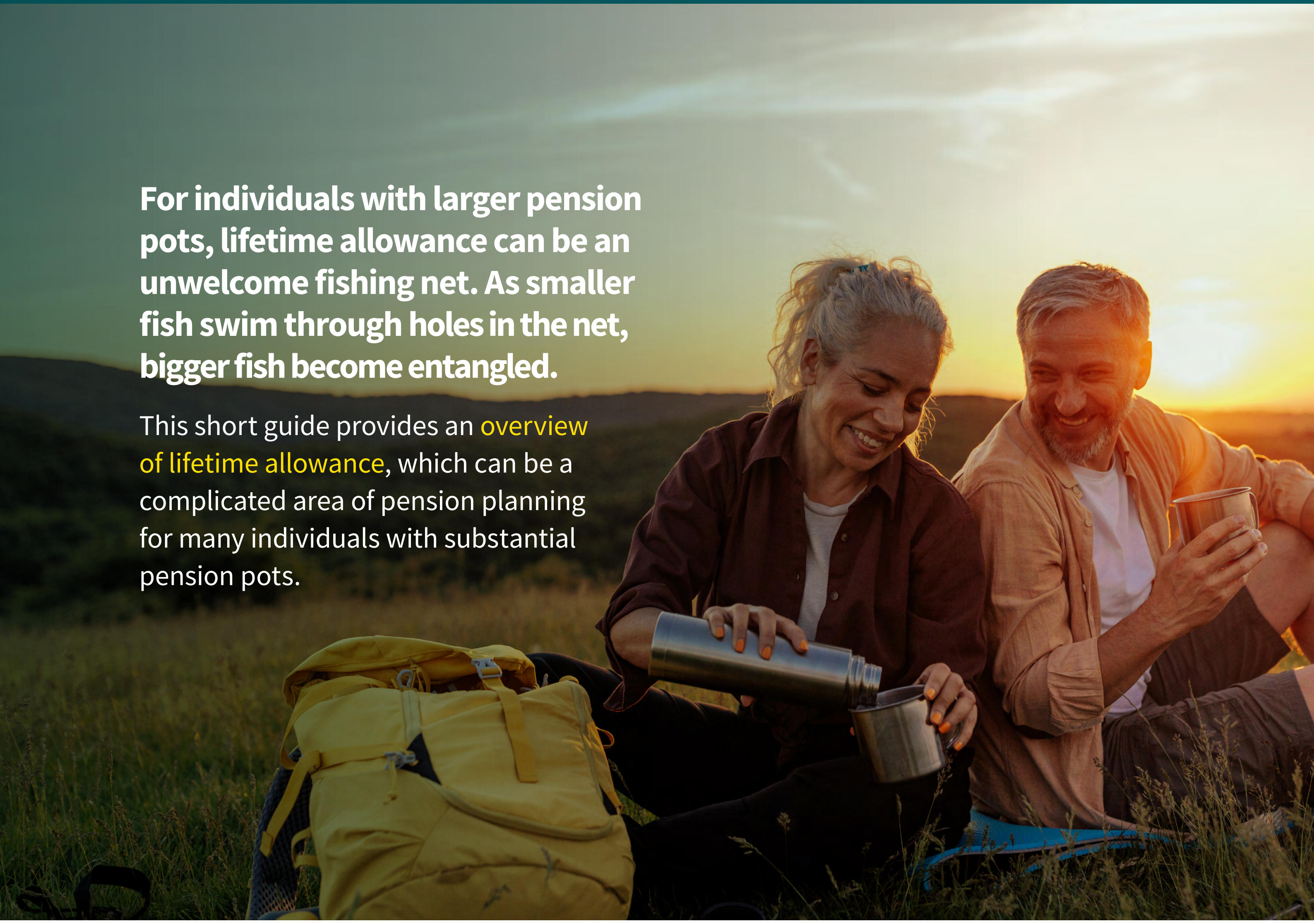
Pension lifetime allowance

What to look out for and
what you can do about it



For individuals with larger pension pots, lifetime allowance can be an unwelcome fishing net. As smaller fish swim through holes in the net, bigger fish become entangled.

This short guide provides an overview of lifetime allowance, which can be a complicated area of pension planning for many individuals with substantial pension pots.

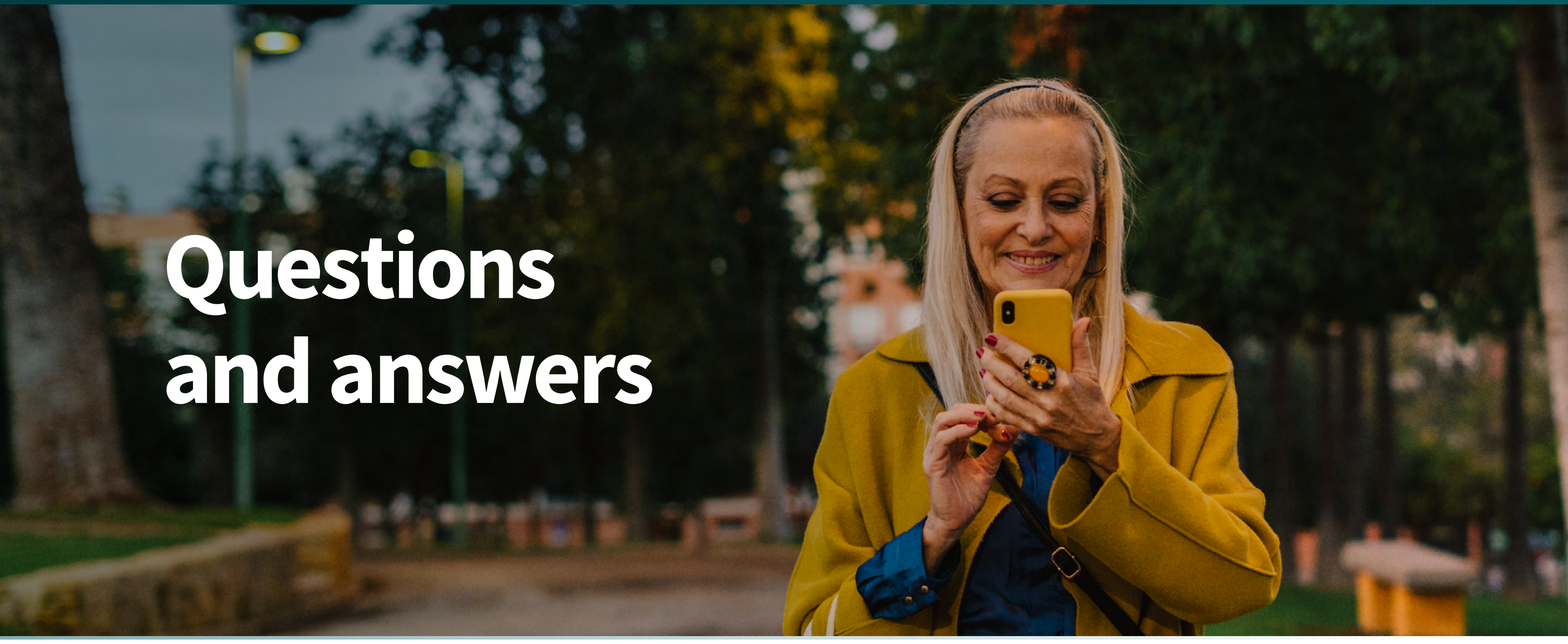
Before you consult a **qualified financial adviser** about this issue, what you read here can act as a **beginner's guide,** helping to answer basic questions, such as:

What is it?

Could it be a **problem for me**, and **when**?

What **actions** can I take to **find out more**?

We hope you find it useful. HMRC's extensive Pensions Tax Manual covers the detail in depth, and where appropriate, we've provided links to the areas we've covered.



Questions and answers

Q What is the lifetime allowance?

A If you save in a pension, you'll have a 'lifetime' allowance. It applies to the value of all types of registered pension schemes that you hold during your lifetime. The 'allowance' refers to the value of tax-privileged benefits they can draw from these pension schemes. It's personal to you, and you can't work your way around it.

But simply having a pension of this size doesn't automatically trigger a tax charge. As ever, the devil is in the detail, and there's plenty of it to consider.

The first thing to get straight is that there's no limit to how much you can save in a pension, so the lifetime allowance is certainly not something to stop you saving for you retirement.

It's just that when your pension's value exceeds a specific figure, and certain things happen to it, a tax charge can be triggered. Effectively, it claws back some of the tax reliefs you've accumulated while building the pension pot in the first place.

The **lifetime allowance** has **reduced over time**

and currently it's

£1,073,100

though the government has announced that it intends to abolish the lifetime allowance on 6 April 2024

In 2006

When it was first introduced it was

£1,500,000

Q When is a charge triggered?

A That can happen when what's known as a 'benefit crystallisation event' (BCE) occurs and there are two main occasions that trigger it:

- when you start to take benefits from a pension
- when you die.

In certain circumstances, it's more complicated than that. HMRC currently lists 13 specific situations in which these events could happen if benefits in excess of the lifetime allowance are paid as a lump sum.

And just in case you need more detail, you'll find it here: **PTM088100 - The lifetime allowance and the lifetime allowance charge: benefit crystallisation events: benefit crystallisation events overview - HMRC internal manual** - GOV.UK (www.gov.uk)

Q So how can I work out if my pension pot will be affected by this?

A The first thing to do is to get information about the size of your pension pots, added together. For that, it's useful to know how big the lifetime allowance 'net' is, and what the size of the catch includes. The 'catch' applies to the two main types of UK pension schemes, defined contribution and defined benefit (or 'final salary') pensions.

Here's a rough guide to what's in scope:

For **defined contribution schemes**
(covering most private and workplace pensions)

That's all the money allocated to you that comes from either **your contributions** and/or **your employer**.

For **defined benefit pensions**
the calculation is different.

It's how much pension you'd get in your **first year** of taking it, **multiplied by 20** + a lump sum

But given the variety and complexity of some older pension schemes, these are not hard and fast rules, so knowing how much you have can be difficult.

Q What's my best option in this situation?

A A simple rule is to keep an eye on the value of all your pension schemes because it's best to be prepared. For example, defined contribution schemes are normally linked to the returns from investment markets, which can fall and then rise in value just as dramatically. Consequently, you could find that your pension assets have dipped you in the lifetime allowance 'net' without your knowledge.

For many people, it can be a surprise when the figures are added up. Your best bet is to keep on top of things. And you can always ask whoever provides your pension how much of your lifetime allowance you've used up. That will save you the time of wading through the paperwork. It's also an area where professional financial advice may be welcome.

Q So as soon as a ‘benefit crystallisation event’ (BCE) occurs, I’m liable for a tax charge?

A Not necessarily. You would normally pay tax if your various pensions were collectively worth more than the lifetime allowance, and the excess was paid to you as a lump sum. However, you might be able to ‘protect’ your pension pot from reductions to the lifetime allowance. Remember that we mentioned that the lifetime allowance had gradually reduced since 2012, having increased after its introduction. This brought more pension pots into the tax charge ‘net’?

You might already have one of these lifetime allowance protections in place. HMRC will allocate a protection reference number to it.

Q What are the ‘lifetime allowance protections’?

A Basically, there are four main types of lifetime allowance protections: primary; enhanced; fixed; and individual. You can also apply to HMRC for an enhancement factor in certain circumstances, including where your pension benefits have been shared following a divorce, or after you’ve transferred benefits to the UK from an overseas pension scheme.

The **good news** is that you can apply **to protect** your lifetime allowance from this expanding ‘net’ through what are known as lifetime allowance protections.

The outcomes can be

- You can take benefits in excess of the lifetime allowance
- Your charge is reduced
- You don’t pay a lifetime allowance charge

Lifetime allowance protections

Some individuals will have more than one type of protection in place, so things can become complicated. So how you protect your specific pension or pensions isn’t something we can answer here, as there are so many potential variables.

HMRC provides the detail on each type of protection. To get to grips with it, here’s where you’ll find the information. As you’ll see, it’s primarily – although not exclusively – helpful for those with an extensive knowledge of pension schemes. You can still apply for Fixed and Individual Protection 2016, and for protection factors that apply to your personal situation:

1. **Primary**
   Protects pre-April 2006 pension rights.
   PTM092300
2. **Enhanced**
   Protects pre-April 2006 pension rights.
   PTM092400
3. **Fixed**
   You can **apply for this protection** if you have not made any pension contributions since 5 April 2016.
   PTM093000
4. **Individual**
   This offers **more flexibility** than fixed protection as it doesn’t restrict future pension savings.
   PTM094000
5. **Divorce and International**
   For divorce; international non-residence; and transfers from recognised overseas pension schemes to UK registered pension schemes.
   For divorce: PTM092200
   For overseas: PTM095400

All these forms of protection are complex. It’s an area where suitable professional advice is essential.

Q I'm ready to take my pension benefits. What should I look out for?

A When you're ready to take your pension benefits and you have lifetime allowance protection, tell your pension provider the type of protection you have and its protection reference number.

Your provider might then ask you about other pensions you have, to check your lifetime allowance status.

You may also need to send them **any certificate** that **HMRC sent you.**

Q So, it's up to me to check that I have protection?

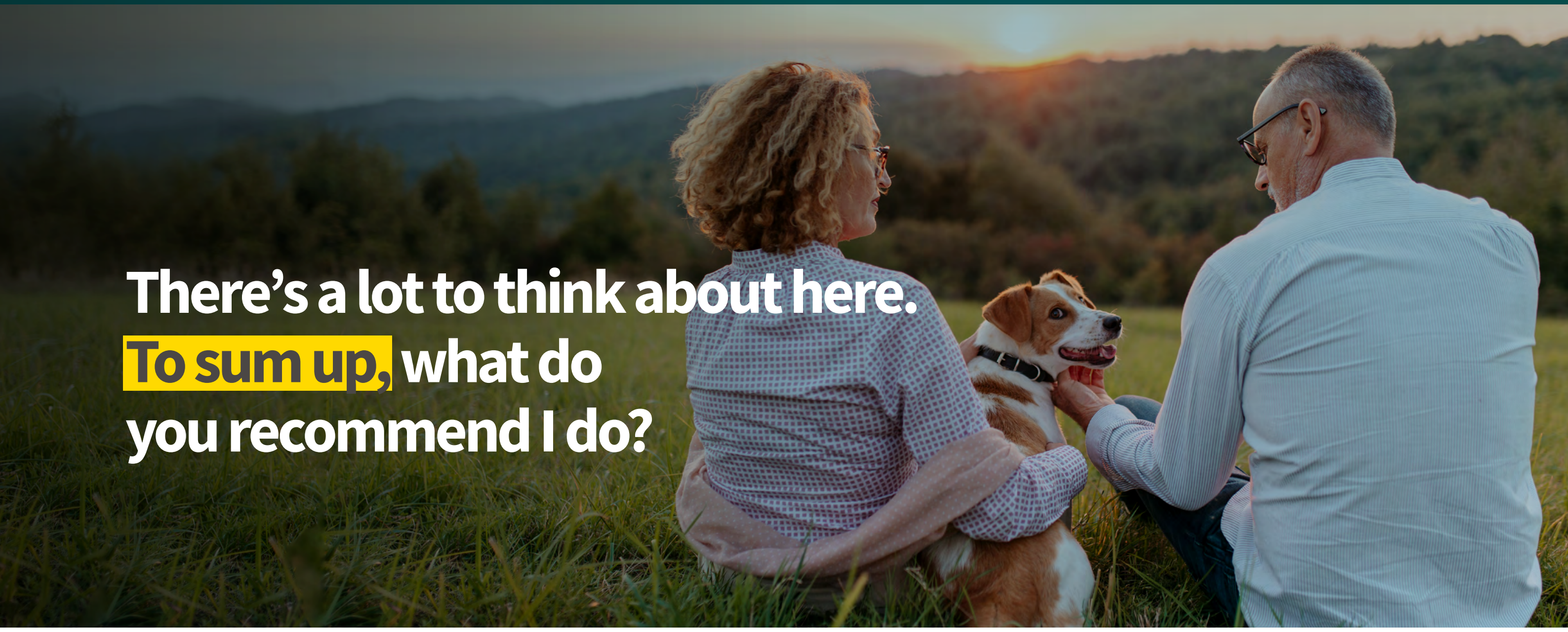
A It certainly is and we can't emphasise it enough. If you neglect to check that you have protection and then fail to let your pension provider know the details, you may well end up paying tax on any lump sum you receive that is in excess of your known lump sum allowance. It's very much about individuals providing the information and thinking carefully before deciding to take their pension benefits.

Q Would I pay tax and how much is it?

A It depends on your personal circumstances, but if you go over your lifetime allowance, your pension provider will deduct any tax due.

You must then complete a HMRC Self Assessment tax return to record the tax deducted from your pension.

When it's paid to you, all pension value is taxable at your marginal rate other than PCLS within the relevant allowance. This means that lump sums in **excess of 25%** of your available LTA (or your lump sum allowance if higher) are immediately taxed at your marginal rate. All other pension income is taxed under PAYE regulations when it's released to you.



There's a lot to think about here. To sum up, what do you recommend I do?

You're an important individual among thousands of people who will read this document. Some of you will act as soon as possible, while some will take notes for the future. Some will consult an independent financial adviser. Given the diverse nature of pension arrangements, each person's situation will be unique.

However, there are three things that anyone in this situation should do, regardless of their current financial situation: **review, record, and report**.

Review

It's often easy to **'file and forget'** the information you receive from **pension schemes**,

but when you accumulate substantial assets, it's important to monitor their value. With defined contribution schemes, it's relatively straightforward. With defined benefit arrangements, it's a little more complicated.

Record

Takes notes of your **scheme reference numbers**, the dates you started and finished them.

Your protection reference number is particularly important. All these digits and dates will be helpful when it comes to the lifetime allowance. The way that pension documents are issued, there's often a lot of paperwork to wade through to find that elusive percentage figure relating to the lifetime allowance.

Report

If you **go over** your lifetime allowance you **must report changes** to HMRC.

For example, you could lose enhanced protection or fixed protection if you did certain things before 6 April 2023, such as: save in a new pension arrangement; enrol in a new workplace pension; or if you transfer certain pensions with paying attention to the rules. You simply need to keep HMRC informed, either online or by post.

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