

## The Lifetime Allowance

This factsheet outlines the current lifetime allowance rules. The government has reduced the lifetime allowance to £1 million with effect from 6 April 2016.

**The Pensions Advisory Service is unable to give individual specific advice and you should seek alternative tax or independent financial advice.**



### What is the lifetime allowance?

The lifetime allowance is the maximum amount of tax relieved pension savings you can build up over your lifetime. It is set by government and reviewed regularly. It is set at a high level, so it is unlikely that you will be affected by it.

Whenever benefits are taken from a pension, you use up a percentage of the lifetime allowance. This is known as a Benefit Crystallisation Event (BCE). A BCE arises in the following circumstances:

- Entering drawdown BCE1
- Entering scheme pension BCE2
- Scheme pension in payment increasing beyond a permitted margin BCE3
- Entering a lifetime annuity BCE4
- Reaching age 75 before taking all benefits from a defined benefit pension BCE5
- Reaching age 75 with a drawdown fund BCE5A
- Reaching age 75 before taking all benefits from a defined contribution pension BCE5B
- Funds on death under age 75 being used to provide drawdown for dependant/nominee BCE5C
- Funds on death under age 75 being used to buy an annuity for dependant/nominee BCE5D
- Taking pension commencement lump sum (tax-free cash) BCE6
- Fund on death under age 75 being paid as a lump sum (BCE7)
- Transferring to a Recognised Overseas Pension Scheme (ROPS) (BCE8)
- Various one-off payments as prescribed in regulations (BCE9)

The value of a BCE is normally the amount paid out or moved to provide retirement income. For defined benefit pensions, the value is normally treated as 20 times the initial amount of pension plus any tax-free cash.

If you are unsure whether or not your current pension savings will exceed the lifetime allowance, you should speak to your pension provider, scheme administrator or seek financial advice.

## Changes to the lifetime allowance

The lifetime allowance for the 2015/16 tax year is £1.25 million and the government will reduce this to £1 million for the 2016/17 tax year.

Additionally, from April 2018, the lifetime allowance will be indexed year on year in line with the Consumer Price Index.

### Am I already protected against the lifetime allowance?

Protection is designed to shelter large pension funds, in part or in full, from the effects of the lifetime allowance charge. It was possible to register for protection when it was introduced in April 2006 and when it decreased in 2012 and 2014.

The main protections are:

- Enhanced protection - available when choosing not to pay into pension funds after 5 April 2006. Funds are not subject to the lifetime allowance.
- Primary protection - available when pension funds were valued in excess of £1.5 million at 5 April 2006. The lifetime allowance will be 1.2 times the value of the funds at that date. Payments into the funds can continue.
- Fixed protection 2012 – available when choosing not to pay into pension funds after 5 April 2012. The lifetime allowance remains at £1.8 million.
- Fixed protection 2014 available when choosing not to pay into pension funds after 5 April 2014. The lifetime allowance remains at £1.5 million.
- Individual protection 2014 – available when pension funds are valued in excess of £1.25 million as at 5 April 2014. The lifetime allowance remains at this value, subject to a maximum of £1.5 million. Payments into the funds can continue.

If you have any of the existing lifetime allowance protections (such as primary or enhanced protection, fixed protection 2012, fixed protection 2014 or individual protection 2014), you will automatically keep this protection when the lifetime allowance is reduced. You do not have to take any further action.

### What new protections are available in 2016?

As of April 2016 you are able to apply for one of or both of the following protections:

- Fixed protection 2016 (FP2016) is available for those that do not already have a previous version of fixed, enhanced or primary protection and do not contribute into or accrue benefits after 5th April 2016. The lifetime allowance will be £1.25 Million or the lifetime allowance at the time, whichever is higher.
- Individual protection 2016 (IP2016) is available for those that have a total relevant amount of their pensions valued in excess of £1 Million as at the 5th April 2016, and protects them to that amount up to a maximum of £1.25 Million.

The total relevant amount is the sum of amounts A to D below all valued as at 5 April 2016:

- A. The amount of pensions in payment before 6 April 2006 (A-Day)
- B. The amount of benefits crystallised between 6 April 2006 and 5 April 2016
- C. The amount of uncrystallised UK registered pension savings
- D. The amount of uncrystallised relieved non-UK pension savings

The calculation can be complicated so we have set out some straightforward examples below to assist you relating to each of the 4 items above. If your position is more complex it is recommended that you obtain independent financial advice to clarify your position, to help to ensure that you do not get an unexpected tax bill.

## What new protections are available in 2016? (cont.)

### Item A

#### **How to value a pre-A Day pension in payment if there have been no Benefit Commencement Events (BCEs) since A Day**

If you have a pension in payment pre A-Day (item A above), for protection purposes it's valued as the amount of pension in force at that date x 25, so you will need to take account of any annual increases to your pension. So for instance, if you have a pension of £25,000 p.a. payable at the date you apply for protection, then the amount to include when applying for protection would be; £25,000 x 25 = £625,000.

#### **How to value a pre-A Day pension in payment if there has been a Benefit Commencement Events (BCEs) since A Day**

If you have a pension in payment pre A-Day (item A above), then you need to work out the value at the date of first BCE. It's valued as the amount of pension in force at that date x 25. So you will need to take account of any annual increases to your pension to the date of the first BCE. To work out the value for your application for protection you then need to ratio it by the ratio of £1.25m/Lifetime Allowance at date of first BCE. So for instance, if you had a pension of £25,000 p.a. payable at the date of first BCE, and the Lifetime Allowance at that date was £1.5m, then the amount to include when applying for protection would be; £25,000 x 25 x 1.25/1.5 = £520,833.

#### **If you were in a drawdown policy at A-Day and have remained in "Capped drawdown", then**

The value you use for protection purposes is the maximum you can currently take from your policy, based on the most recent review. Your provider will be able to advise you of this amount. The value to use when applying for protection is this amount x 25.

#### **If you were in a drawdown policy at A-Day but have since converted it to a "Flexi-access drawdown" plan.**

This is a complicated area, and you should seek guidance from your provider as to what amount to use when applying for protection.

### Item B

If you have crystallised benefits after A-Day, you take the amount crystallised at each date and then ratio the amounts by £1.25m/Lifetime Allowances at date of crystallisation. So for instance, if someone crystallised £100,000 when the LTA was £1.8m and £250,000 when the LTA was £1.5m the amount to include in the protection calculation would be: £100,000 x 1.25/1.8 (= £69,444) + £250,000 x 1.25/1.5 (£208,333); Total = £277,777.

### Item C

This is relatively straightforward. If you have a defined contribution fund, you take the actual value of the policy. You will need to check with your provider to get the latest value. For a defined benefit pension, it's the current level of pension you have built up x 20. You may also need to include any lump sum entitlements on top of this, if your scheme offers this as well (note – this is not the 25% tax free cash entitlement you have if you decided to give up a quarter of your pension at retirement). The value of benefit built up will be on your latest benefit statement from your policy. If you are a deferred member, you may need to confirm the latest value with your administrator.

### Item D

This is a complicated area and financial advice will generally be required as there are many complex rules setting out what is within and outside the scope of UK tax rules. As a rule of thumb, if UK tax relief has been available on a policy, then the scheme will have on-going reporting and information obligations that should help you understand the value of the policy for protection purposes.

## How do I apply?

- Before the online application process is launched, between 6 April and July, you can write in using a pro-forma letter to:

Pension Schemes Services  
Fitzroy House  
Castle Meadow Road  
Nottingham  
NG2 1BD

The pro-forma letters can be found in the appendices at the back of HMRC's Pension Schemes Newsletter 76, please see <https://www.gov.uk/government/publications/pension-schemes-newsletter-76-february-2016/pension-schemes-newsletter-76-february-2016>

## What does this mean for me?

Any pension savings above the lifetime allowance are subject to the lifetime allowance charge. This charge will continue to be:

- 55% if the excess is taken as a lump sum
- 25% if the excess is taken as income, for example as a scheme pension, an annuity or drawdown. Income tax at your marginal rate will also be payable.

## What are HMRC's comments?

You can find more information about the reduction of the lifetime allowance in Pension Schemes Newsletters 75, 76 and 77

<https://www.gov.uk/government/publications/pension-schemes-newsletter-75-january-2016/pension-schemes-newsletter-75-january-2016>

<https://www.gov.uk/government/publications/pension-schemes-newsletter-76-february-2016/pension-schemes-newsletter-76-february-2016>

<https://www.gov.uk/government/publications/pension-schemes-newsletter-77-march-2016/pension-schemes-newsletter-77-march-2016>

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We help with all pension matters covering workplace, personal and stakeholder schemes and also the State Pension. We answer general questions, help with specific queries and offer guidance for people with complaints about their private pension scheme.

### Contacting us



Pensions Helpline  
(Monday- Friday 9:00am- 5:00pm)

**0300 123 1047**



Online enquiry form

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