HARGREAVES LANSDOWN

LIFETIME ALLOWANCE GUIDE

2023/24 tax year

IMPORTANT INFORMATION

This guide is based on our understanding of current and proposed legislation as at 6 April 2023, which is subject to change. All figures, unless stated, apply to the 2023/24 tax year. Any tax benefits or charges will depend on your circumstances. This guide isn't personal advice. If you're not sure what's right for your situation, please ask for advice.

LIFETIME ALLOWANCE RULES

> The lifetime allowance is measured each time you take money from your pension, at age 75 or if you die before 75 without accessing your pension.

There's a limit on the total value of pension benefits you can build up throughout your lifetime (this includes employer pension schemes) and generally receive up to 25% tax free. This limit is known as the lifetime allowance. Unless you have protection, the standard lifetime allowance is currently £1,073,100.

Under the old rules, if your pension value grew to beyond the standard lifetime allowance it would trigger a tax charge. But since 6 April 2023, the lifetime allowance charge has been removed. And from April 2024, the lifetime allowance is set to be completely abolished.

WHEN IS THE LIFETIME ALLOWANCE MEASURED?
Whenever you take benefits from a pension, you use up a percentage of the lifetime allowance. This is called a Benefit Crystallisation Event (BCE).

For example, a pension fund worth £107,310 from which you take benefits in 2023/24 will use up 10% of the lifetime allowance. On the next page, you'll find other times that your allowance will be measured.

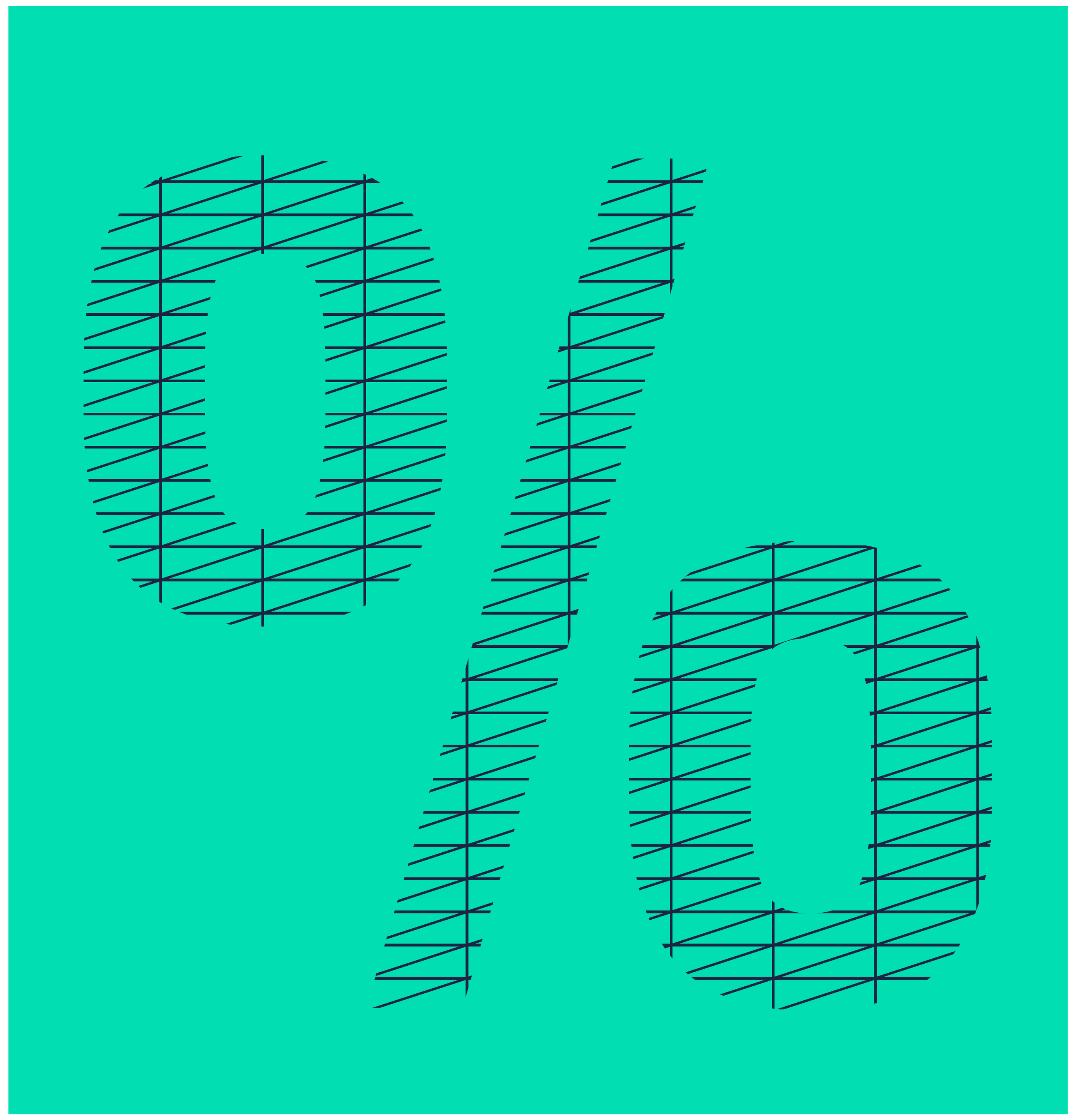
Up to

25%

tax free

- When you use your pension fund to buy an annuity, move into drawdown, take an uncrystallised funds pension lump sum or take tax-free cash before 75. The percentage is based on the value of the pension fund used. If you buy an annuity from drawdown, only the value above the amount you moved into drawdown is taken into account.
- When you start to receive tax-free cash and/or a pension from a defined benefit pension scheme before 75. The percentage is based on the annual pension payment and tax-free cash amount.
- When you reach 75 with pension benefits which you haven't taken or which are in drawdown. For drawdown funds, only the value above the amount you moved into drawdown is taken into account. If the drawdown fund value at 75 is lower than the amount originally moved into drawdown then no additional lifetime allowance will be used.
- If you die before 75 without having taken benefits from the pension. The percentage is based on the value of the fund. Life cover/insurance written under pension rules may also be included.
- If you transfer to a Qualifying Recognised Overseas Pension Scheme before 75. The percentage is based on the value of the transfer. For drawdown funds, only the value above the amount you moved into drawdown is taken into account.
- When you have an excessive increase on a scheme in payment, such as a final salary pension.
- Various one-off payments from a pension scheme may also be measured against the lifetime allowance.

Each time your pension is measured against the lifetime allowance you'll receive a certificate showing the percentage of the standard lifetime allowance this has used (unless you have fixed or individual protection – see page 7).



HOW DO I KNOW IF I AM NEAR THE LIFETIME ALLOWANCE?

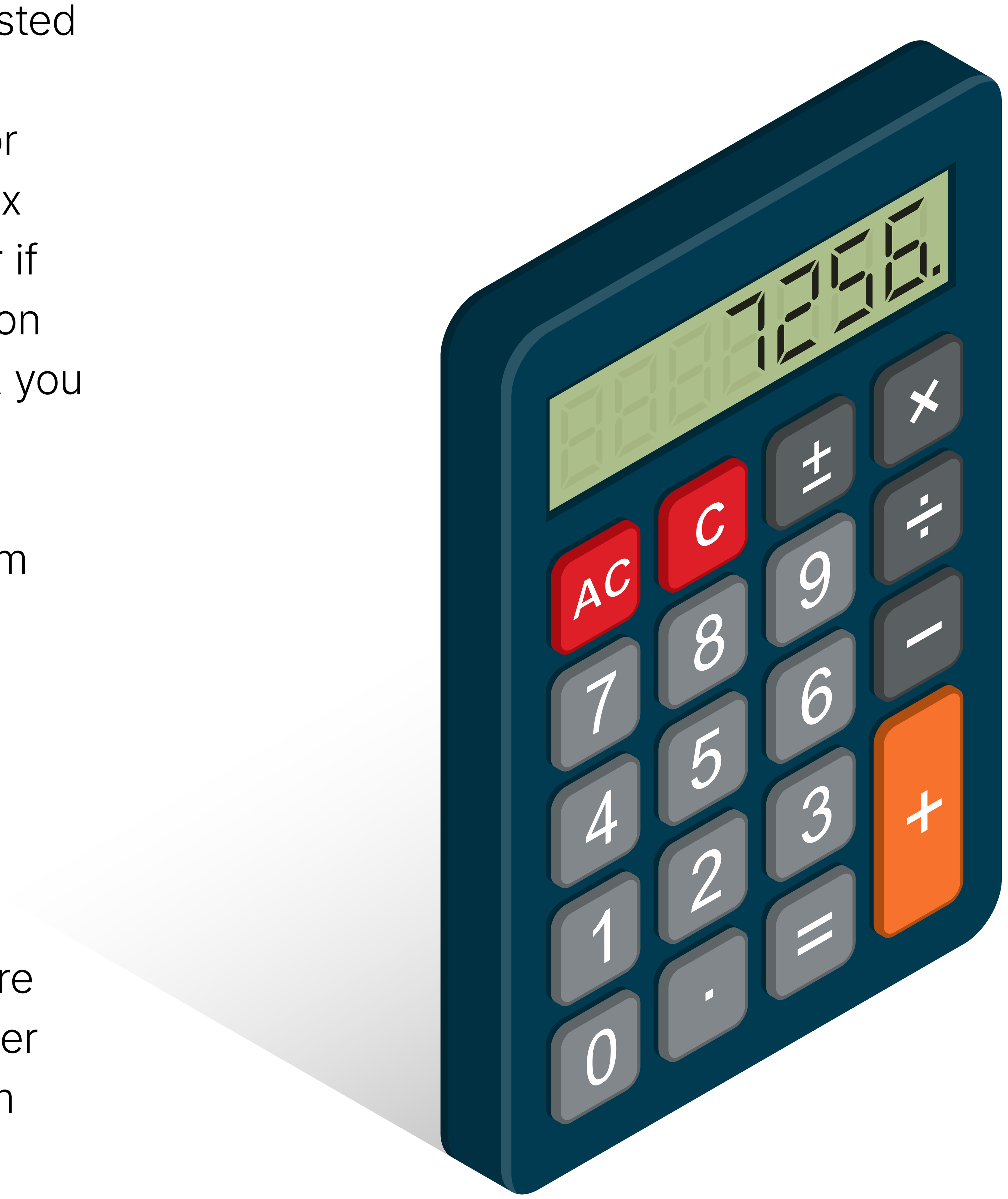
Despite plans to abolish the lifetime allowance, your pensions will still be measured against it. This is because it still provides an upper limit to the tax-free amount that can be typically accessed from pensions.

For this reason, it's important to check whether you're nearing the limit. You should consider the value of all your private and work pensions, calculated as:

- Money purchase pensions (e.g. a SIPP) not yet taken = the current value.
- Defined benefit (e.g. final salary) pensions not in payment = 20 x the annual pension due, plus any additional tax-free cash.
- Pensions taken since 5 April 2006 = the percentage of the lifetime allowance used up, as stated by that pension provider. This percentage does not change when the lifetime allowance changes (although if you hold primary protection – see page 10).
- Pensions taken before 6 April 2006 were not tested at that time, but they are tested at the time you first access any other pension benefits after 5 April 2006. For scheme pensions or annuities, use 25 x the annual pension you're receiving, or if you've already accessed further pension benefits after 5 April 2006 the amount you were receiving at that time.

For drawdown this is 25 x the maximum income you could take, or could have taken at the time you first accessed further pension benefits after 5 April 2006 (for flexible drawdown this is the maximum which would have applied when you converted). If however, you have a drawdown pension set up before April 2006 and haven't taken any further benefits you should use 20 x maximum income if:

- you're in capped drawdown;
- you converted to flexible drawdown after 5 April 2015. This is the maximum which would have applied when you converted;
- you converted to flexible drawdown before 6 April 2015 in a pension year which started after 26 March 2014. This is the maximum which would have applied when you converted.



WHAT WILL MY PENSION PROVIDER NEED TO KNOW?

When you take benefits from a pension your provider will need to know if it will put you over the lifetime allowance, and therefore typically ask:

- Have you started to take pension benefits since 5 April 2006? If so, what percentage of the lifetime allowance have you already used? This figure is on the certificate issued when taking benefits.
- If not, are you receiving any pensions that started before 6 April 2006? If so, they will ask for the latest annual income. If in drawdown, they will need to know the appropriate amount to take into account – see ‘How do I know if I am near the lifetime allowance?’ section. They may also need additional information.

Alternatively, they may simply ask you whether you’re likely to exceed the lifetime allowance by taking these benefits.

WHAT HAPPENS IF I GO OVER THE LIFETIME ALLOWANCE?

Most people’s pension wealth won’t grow to be more than their lifetime allowance. But if you’re does, there are some things to be aware of.

From 6 April 2023, the lifetime allowance charge was removed. Any lump sum payments which would have been taxed at 55%, due to being over the lifetime allowance, will instead be taxed at your marginal rate of income tax.

You can choose to:

- Take the excess as a lump sum before 75, less income tax at your marginal rate.
- Keep the excess in the pension fund, before or after 75. If you take money out of the pension later, the excess will be taxed as income.

TAX-FREE CASH

The maximum tax-free cash is normally limited to the lower of 25% of the benefits being taken and 25% of your remaining standard lifetime allowance. When calculating your remaining standard lifetime allowance for this purpose, after reaching age 75, you should ignore any lifetime allowance used up by pensions from which you had not taken benefits at age 75. But you should include any pension benefits taken after 75 as if they used up the lifetime allowance. Some people have lifetime allowance and/or tax-free cash protection which can increase the available tax-free cash.

PROTECTION AGAINST THE LIFETIME ALLOWANCE

Even though the lifetime allowance charge no longer applies, you might consider applying for protection if you're nearing the lifetime allowance (currently £1,073,100). By applying for protection, you could be entitled to a higher tax-free amount.

There are generally only two types that you can still apply for, if eligible. These are fixed protection 2016 and individual protection 2016. There is currently no deadline for applying, although there is no longer a requirement on schemes to provide a valuation for the purposes of applying for individual protection 2016.

To apply on the HMRC website you need an HMRC Online Services account – you can create this when applying. You won't be given a certificate but can print your details. If you cannot apply online contact HMRC on **0300 123 1079**.

If you apply for fixed protection after 14 March 2023, you'll be unable to accrue further benefits (e.g. make further contributions), join new pension arrangements and make certain types of transfer without losing your protection.

WHAT IF I ALREADY HAVE LIFETIME ALLOWANCE PROTECTION?

Those who hold valid protection could be entitled to a higher tax-free amount. In addition, from 6 April 2023, those who applied for enhanced or any of the fixed protections prior to 15 March 2023 (and were successful in their application), will be able to accrue new pension benefits (e.g. make further pension contributions) join new pension arrangements and make certain types of transfer without losing the protection.

Fixed protection 2016

This fixes your allowance at £1.25 million. You can only apply for this protection if no pension benefits were accrued after 5 April 2016 – this includes personal and employer contributions and building up further benefits in a final salary scheme.

Those who applied for this protection prior to 15 March 2023 (and were successful in their application) will be able to accrue new pension benefits from 6 April 2023 without losing the protection.

Those who apply after 14 March 2023 (and are successful in their application) will lose the protection by taking certain actions, which include accumulating further benefits, joining new pension arrangements and making certain types of transfer.

You can only apply if you do not have protection from a previous year, other than individual protection 2014 (see below).

Fixed protection 2016 could allow you to benefit from a higher tax-free cash amount of up to £312,500.

Individual protection 2016

This fixes your allowance at the value of your pensions as of 5 April 2016, up to a maximum of £1.25 million. You can continue to make and receive contributions. You will only qualify for individual protection 2016 if your pensions were worth more than £1 million in total as of 5 April 2016, and you do not hold primary protection or individual protection 2014.

Individual protection 2016 could allow you to benefit from a higher tax-free cash amount of up to £312,500, depending on the value of your protected allowance.

Enhanced protection – April 2006

In rare cases you might be able to apply for enhanced protection, but it's very unlikely. Enhanced protection allowed people to take pension benefits without ever triggering a lifetime allowance tax charge, although they couldn't accrue further pension benefits after 5 April 2006 without losing the protection.

However, from 6 April 2023, those who applied for enhanced protection prior to 15 March 2023 (and were successful in their application), will be able to accrue new pension benefits (e.g. make further pension contributions), join new pension arrangements and make certain types of transfer without losing the protection.

Holders of enhanced protection may also benefit from a higher tax-free entitlement because of the protection.

If you hold enhanced protection without tax-free cash protection, the maximum tax-free cash will be calculated by reference to the higher of the standard lifetime allowance and £1.5 million.

Prior to 6 April 2023, if you had enhanced protection with tax-free cash protection, the percentage displayed on the certificate was the maximum amount that could normally be taken tax-free each time benefits were taken.

However, from 6 April 2023, the percentage that can be taken tax-free will be capped based on the value of the pension as at 5 April 2023. Effectively excluding any contributions made on or after 6 April 2023 for the purpose of calculating the maximum tax-free cash.

Enhanced protection – Example 1

Let's say someone holds valid enhanced protection (applied for on 5 January 2009), with lump sum protection of 40%. Their pension would be valued on 5 April 2023 to calculate the maximum tax-free cash amount at that time. If their pension was valued at £1.75 million, they would be entitled to a higher tax-free cash amount of £700,000.

When they came to take benefits from their pension, even if their pension value had grown over £1.75 million, they'd still only be entitled to 40% tax-free cash of the pension value on 5 April 2023 (£700,000).

Enhanced protection – Example 2

Let's say someone holds enhanced protection (applied for on 2 February 2009), with lump sum protection of 40%. Their pension would be valued on 5 April 2023 to calculate the maximum tax-free cash amount at that time. If their pension was valued at £1.6 million, they would be entitled to a higher tax-free cash amount of £640,000.

However, when they came to take benefits from their pension their pension value had decreased in value to £1.5 million, so they'd only be entitled to a maximum tax-free cash amount of £600,000 (40% of £1,500,000).

You can find details of whether you have enhanced protection with or without tax-free cash protection on your certificate (if you have tax-free cash protection this will be displayed as a percentage on the certificate).

April 2006 – primary protection

In rare cases you might be able to apply for primary protection, but it's very unlikely.

For those that already hold primary protection, the recent rule changes haven't affected your tax-free cash entitlement. Your primary protection certificate will still show a primary protection factor representing the additional amount of lifetime allowance to which you're entitled.

From 6 April 2012 this factor is applied to the higher of the standard lifetime allowance and £1.8 million. For example, if the factor shown is 2, you are entitled to 2 x £1.8 million plus £1.8 million, i.e. a total of £5.4 million. Benefits taken since April 2006 will have used a percentage of the lifetime allowance. Each time benefits are taken; any previous BCEs are revalued in accordance with HMRC rules.

In terms of tax-free cash, if you have primary protection but no tax-free cash protection, the maximum tax-free cash will be calculated by reference to the higher of the standard lifetime allowance and £1.5 million.

If you have tax-free cash protection as part of your primary protection, then you'll have a figure printed on your certificate telling you what your protected tax-free cash amount is.

Under the current rules, that amount will be increased by 20%. Any tax-free cash taken since 6 April 2006 will be revalued as if the current lifetime allowance was £1.8 million.

Primary protection – Example

Let's say someone holds valid primary protection with a tax-free cash protection figure of £400,000, Under the current rules the maximum tax-free cash amount would be £480,000 (£400,000 + (£400,000 x 20%)).

2012 and 2014 – fixed protection

On 6 April 2012 the standard lifetime allowance fell from £1.8 million to £1.5 million. Individuals with no other protection were able to apply (until 5 April 2012) to fix their lifetime allowance at the higher of £1.8 million or the standard lifetime allowance.

People with this protection could benefit from a maximum tax-free cash amount of up to £450,000.

On 6 April 2014 the lifetime allowance fell from £1.5 million to £1.25 million. Individuals with no other protection were able to apply (until 5 April 2014) to fix their lifetime allowance at the higher of £1.5 million or the standard lifetime allowance.

People with this protection could benefit from a maximum tax-free cash amount of up to £375,000.

When your pension is measured against the lifetime allowance while holding fixed protection, you use up a percentage of your personalised lifetime allowance. The recent rule changes don't change the way in which the maximum tax-free cash is calculated for these protections.

However, from 6 April 2023, individuals with these protections will be able to accrue new pension benefits (e.g. make further pension contributions), join new pension arrangements and make certain types of transfer without losing the protection.

Fixed protection – Example 1

Let's say someone holds fixed protection 2014 and has never taken pension benefits before. If their pension was worth £1,275,000 and they contributed £25,000 after 5 April 2023, that would bring the total value of their pension to £1,300,000. If they then wanted to move the whole of their pension into drawdown, the maximum amount that could be taken tax-free would be £325,000 (25% of £1,300,000).

Fixed protection – Example 2

Let's say someone holds fixed protection 2012 and has never taken pension benefits before. If their pension was worth £2,000,000 and they wanted to move the whole of their pension into drawdown, the maximum amount that could be taken tax-free would be £450,000 (25% of their lifetime allowance of £1.8 million). The remainder would be taxed as income at their marginal rate at the point it was withdrawn.

2014 – individual protection

If your pensions were worth at least £1.25 million on 5 April 2014, you were able to apply for individual protection 2014. It set your allowance at the value of your pensions at 5 April 2014, up to £1.5 million, and allowed you to continue making contributions. When your pension is measured against the lifetime allowance, you use up a percentage of your personalised lifetime allowance. Applications for individual protection 2014 closed on 5 April 2017. The method used to calculate the maximum tax-free cash for this form of protection is unchanged.

This means you could benefit from a higher tax-free cash amount of up to £375,000, depending on the value of your protected allowance.

Individual protection – Example 1

Let's say someone holds individual protection 2014 with a protected value of £1.3 million and has never taken pension benefits before. If their pension was worth £1.25 million at the point, they wanted to move all the funds into drawdown, the maximum amount that could be taken tax-free would be £312,500 (25% of £1.25 million).

Individual protection – Example 2

Let's say someone holds individual protection 2014 with a protected value of £1.5 million and has never taken pension benefits before. If their pension was worth £1.8 million at the point, they wanted to move all the funds into drawdown, the maximum amount that could be taken tax-free would be £375,000 (25% of their personal lifetime allowance of £1.5m). The remainder would be taxed as income at their marginal rate at the point it was withdrawn.

GET HELP FROM AN EXPERT

A financial adviser can help you to gain a deeper understanding of how the changes to the lifetime allowance and pension protection apply to you.

They can tell you:

- Whether you could or should start making pension contributions
- How to plan withdrawals tax efficiently
- The specific impacts on any pension protections you may have
- How you could save tax in other ways

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We're Hargreaves Lansdown – a secure, FTSE 100 company helping UK savers and investors for over 40 years.

Our clients like our wide investment choice, and how easy it is to manage their pension online and with our mobile app. Our Pensions Helpdesk is here six days a week to give you support and answer your questions.

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