

# ANNUAL ALLOWANCE: WHAT YOU NEED TO KNOW

## WHAT IS THE ANNUAL ALLOWANCE?

The annual allowance is the maximum you or someone else, e.g. your employer, can contribute to all your pensions in one year, without incurring a tax charge.

For the 2025/26 tax year the annual allowance is £60,000, although there are three exceptions:

1. If you have accessed a pension since 6 April 2015, or have ever been in flexible drawdown, a reduced contribution limit may also apply. See **"How does the money purchase annual allowance work?" (below)**
2. If your 'adjusted income' is more than £260,000 in the 2025/26 tax year, your annual allowance could be tapered down to as little as £10,000. Broadly speaking this is your total taxable income plus the value of any employer pension contributions. See **"How does the tapered annual allowance work?" (page 2)**
3. If you take benefits from a pension due to what HMRC considers 'serious' or 'severe' ill health, you may not be limited by the annual allowance for the tax year in which you take benefits, even if you would otherwise be caught.

## HOW IS THE ANNUAL ALLOWANCE MEASURED?

To work out how much annual allowance you have used already, you need to calculate the value of all pension contributions made in the 2025/26 tax year. How you calculate this will depend on the type of pension you have and personal circumstances.

**Defined contribution pensions** – e.g. personal pensions, self-invested personal pensions (SIPPs) and stakeholder pensions: you must calculate the value of all contributions made by you, your employer, or anyone else on your behalf. This is the gross value, so includes any basic-rate tax relief added.

**Defined benefit pensions** – e.g. final salary schemes: you must contact your pension provider and ask for your 'pension input amount' in the current tax year. The benefits accrued in a defined benefit scheme are given a value which counts towards the annual allowance. This value can be surprisingly large so it's important you check.

## WHAT HAPPENS IF I EXCEED THE £60,000 ANNUAL ALLOWANCE?

It may be possible to reduce or eliminate the excess by using 'carry forward' – see page 4. Any excess that cannot be eliminated will be added to your income and taxed at your highest rate. This charge should be declared and paid through your income tax self assessment. If the charge is over £2,000 and you have exceeded £60,000 in a single pension, you could instead choose to have it deducted from your pension scheme.

## HOW DOES THE MONEY PURCHASE ANNUAL ALLOWANCE WORK?

Contributions to money purchase plans (e.g. personal pensions), including employer, employee and personal contributions, will become restricted if you flexibly access your pension. The money purchase annual allowance is £10,000 for the 2025/26 tax year.

### Flexibly accessing a pension includes:

- Having flexible drawdown before 6 April 2015
- Exceeding income limits from drawdown set up before 6 April 2015
- Taking an uncrystallised funds pension lump sum (UFPLS) or standalone lump sum
- Taking an income payment from most drawdown arrangements set up after 5 April 2015

- Taking an income payment from drawdown converted to flexible drawdown after 5 April 2015
- Receiving an income payment from a scheme pension with 12 or fewer members or from a flexible annuity

### Flexibly accessing a pension doesn't include:

- Taking a pension arrangement as a small lump sum due to it being worth less than £10,000
- Taking income from capped drawdown set up before 6 April 2015 which remains within capped drawdown limits
- Taking tax-free cash and no income
- Taking a pension as an annuity or scheme pension other than as described above

The money purchase annual allowance doesn't apply to contributions made before you flexibly access your pensions, even if this is part way through a tax year, nor in a tax year in which you take benefits from a pension while in 'serious' or 'severe' ill health.

Unlike with the annual allowance, where it may be possible to carry forward unused allowance from previous years, it's not possible to carry forward the money purchase annual allowance.

## WHAT HAPPENS IF I EXCEED THE £10,000 MONEY PURCHASE ANNUAL ALLOWANCE?

Any excess will be added to your income and taxed at your highest rate. This excess will not count towards the annual allowance. This charge should be declared and paid through your income tax self assessment.

## IMPORTANT INFORMATION

This factsheet is for your information only and is not personal advice. It is based on our current understanding of legislation and HMRC guidance which can change. This is correct for the 2025/26 tax year as of 11 March 2025. If you're in any doubt whether a particular course of action is suitable for your circumstances, you should ask for personal financial advice.

Tax rules can change and any benefits depend on individual circumstances. The value of investments can fall as well as rise, so you may get back less than you invest. If you're unsure any reliefs are applicable to you, you should consult your accountant or HMRC.

# HOW DOES THE TAPERED ANNUAL ALLOWANCE WORK?

The annual allowance is reduced for some people with higher incomes. You are affected if your threshold income is more than £200,000 and your adjusted income level is more than £260,000. Your annual allowance will then depend on your adjusted income. To work out how you might be affected, follow these three steps.

## STEP 1 – CALCULATE YOUR THRESHOLD INCOME

Broadly, threshold income is your total taxable income plus any salary/bonus sacrificed for pension contributions, minus any personal pension contributions you make. To calculate your threshold income:

### A. ADD together your taxable income and some pension contributions

- All taxable income this tax year, for example:
  - Taxable earnings such as salary, bonus and commission (this is the figure after any income sacrificed, for example in exchange for a pension contribution)
  - Most rental income from property
  - Dividend payments
  - Interest on savings
  - Self-employed earnings
- Any salary/bonus sacrificed for pension contributions made this tax year if:
  - The arrangement started, or in some cases is renewed, on or after 9 July 2015; or
  - Contributions are increased on or after 9 July 2015 (this could be the whole amount or just the increase depending on the exact wording of your salary sacrifice agreement)

### B. DEDUCT some reliefs and pension contributions you make this tax year

- Any personal or employee contributions you make to a pension (not employer contributions)
- Any reliefs listed in Section 24 of the Income Tax Act 2007. You may need to speak with an accountant to determine if this is relevant

**If your threshold income is £200,000 or less your annual allowance will not be reduced this tax year.**

**If your threshold income is more than £200,000 this tax year, you might be affected and must next calculate your adjusted income – see step 2.**

## STEP 2 – CALCULATE YOUR ADJUSTED INCOME

Broadly, adjusted income is your total taxable income after any reliefs, plus any employer pension contributions.

To calculate your adjusted income, add together the following from this tax year:

- All taxable income (the same measure used in step 1A)
- Contributions your employer has made to a pension, including any made by salary sacrifice (whenever this was arranged)
- Benefits built up in a defined benefit (e.g. final salary) scheme, excluding the cost of employee contributions
- Contributions you make to occupational/trust-based pension schemes, paid through a net pay arrangement (which would otherwise reduce taxable income)

Then deduct certain reliefs from this tax year (the same reliefs used in step 1B). Don't deduct personal or employee pension contributions.

**If your adjusted income is more than £260,000 your annual allowance will be 'tapered'.**

## STEP 3 – CALCULATE YOUR NEW ANNUAL ALLOWANCE

For every £2 of adjusted income over £260,000, your annual allowance this tax year will be reduced by £1. There are some examples below. For adjusted income over £360,000, your annual allowance will be £10,000 – there is no further reduction.

Adjusted income	Annual allowance
£260,000 or less	£60,000
£310,000	£35,000
£360,000 or more	£10,000

### What happens if I exceed the tapered annual allowance?

It may be possible to reduce or eliminate the excess by using 'carry forward' – see page 4. Any excess that cannot be eliminated will be added to your income and taxed at your highest rate. This charge should be declared and paid through your income tax self assessment. If the charge is over £2,000 and you have exceeded £60,000 in a single pension, you could instead choose to have it deducted from your pension scheme.

### How much could my allowance have been reduced to in previous tax years?

If you think you might be able to 'carry forward' unused allowances from previous tax years (there's more on the carry forward rule on page 4), you'll also need to work out if you were subject to the tapered annual allowance in those tax years if your threshold income was more than £200,000.

To calculate this for tax years 2020/21 to 2022/23, for every £2 of adjusted income over £240,000, your annual allowance would have been reduced by £1. For adjusted income over £312,000, your annual allowance would have been £4,000 – there was no further reduction.

To calculate this for 2023/24 and 2024/25, for every £2 of adjusted income over £260,000, your annual allowance would have been reduced by £1. For adjusted income over £360,000, your annual allowance would have been £10,000 – there was no further reduction.



#### EXAMPLE 1: HARRY

Harry's salary is £210,000.

He makes a personal pension contribution of £17,000. His employer also contributes £17,000.

Harry also owns a buy-to-let property. He receives a taxable rental income of £12,000 each year.

**Threshold income = £205,000**  
(salary + rental income – personal pension contributions)

**Adjusted Income = £239,000**  
(salary + employer contribution + rental income)

As his Adjusted Income is below £260,000, he will not be subject to the taper. This means Harry will have an annual allowance of £60,000.



#### EXAMPLE 2: DIANE

Diane's salary is £240,000.

After contributing 10% to her company pension (via a 'Salary Sacrifice' arrangement which has been in place since 2014), her actual salary is £216,000. Her employer contributes a further 15%.

Diane also holds shares which pay her a dividend income of £10,000 a year.

**Threshold income = £226,000**  
(salary after salary sacrifice + dividend income)

**Adjusted Income = £286,000**  
(salary after salary sacrifice + employer contribution (including those made via 'Salary Sacrifice') + dividend income)

This means Diane's annual allowance will be tapered to £47,000, meaning she has already exceeded this year's annual allowance. She should see if she can reduce or eliminate the excess by using 'carry forward'.



#### EXAMPLE 3: OLIVIA

Olivia's salary is £210,000.

She receives a bonus of £60,000. She takes advantage of this by making a personal pension contribution of £75,000 (using 'Carry Forward').

Her employer also contributes £17,000 to the pension.

**Threshold income = £195,000**  
(total taxable income – personal pension contribution)

**Adjusted Income = £287,000**  
(salary + bonus + employer contributions)

Olivia will not be subject to the taper and so will have an annual allowance of £60,000. This is because, although her Adjusted Income is above £260,000, her Threshold Income is below £200,000.

**All figures and scenarios relate to the 2025/26 tax year and assume no pension withdrawals have been made.**





# CARRY FORWARD: WHAT YOU NEED TO KNOW

## WHAT IS CARRY FORWARD?

It's a rule that lets you take advantage of any unused allowance from the three previous tax years. You can catch up on any contributions that you might have missed in these years.

There are two conditions. First, you must earn at least the amount you wish to contribute in total this tax year (unless your employer is making the contribution). Second, you must have been a member of a UK-registered pension scheme (this doesn't include the State Pension) in each of the tax years from which you wish to carry forward. Membership of any such pension scheme can qualify, even if you didn't make contributions or were already taking benefits.

## WHO COULD POTENTIALLY BENEFIT FROM CARRYING FORWARD UNUSED ALLOWANCE

- ✓ People earning more than £60,000 in the 2025/26 tax year who wish to maximise pension contributions
- ✓ People with an irregular earnings pattern who want to make a large pension contribution in a good year
- ✓ Final salary pension members whose accrued benefits increase significantly and would otherwise incur a tax charge
- ✓ Employers wanting to make large contributions
- ✓ People affected by the tapered annual allowance (page 2)

## HOW DO I WORK OUT HOW MUCH I CAN CARRY FORWARD?

The amount you can carry forward depends on how much unused allowance you have in each of the last three tax years (see table below). Include contributions made by you and your employer, including any benefits accrued in a defined benefit (e.g. final salary) scheme.

Tax year	Annual allowance
2022/23	£40,000*
2023/24	£60,000**
2024/25	£60,000**

\*As low as £4,000 for some people with higher incomes.

\*\* As low as £10,000 for some people with higher incomes

You first use up the current year's annual allowance. You then jump back three years and work progressively forwards.

## CARRY FORWARD EXAMPLE

	2022/23	2023/24	2024/25	2025/26
Annual allowance	£40,000	£60,000	£60,000	£60,000
<b>less</b>				
Total contributions	£30,000	£10,000	£15,000	£0
<b>equals</b>				
Annual allowance remaining	<b>£10,000</b>	<b>£50,000</b>	<b>£45,000</b>	<b>£60,000</b>
<b>Total amount available using carry forward</b>				<b>£165,000</b>

**This is calculated by adding up the remaining annual allowance from 2022/23 through to 2025/26.**

In this example carry forward allows for a contribution of £165,000 without exceeding the annual allowance in 2025/26. The investor would still need £165,000 of earnings in the 2025/26 tax year for this personal contribution to be permitted. This example assumes the investor's allowances are not reduced by the taper (see page 2). The amount you can carry forward will depend on your personal circumstances

## OTHER IMPORTANT POINTS TO CONSIDER

- You can only use unused annual allowance once.
- If total contributions exceeded your annual allowance in any of the last three tax years you cannot carry forward any allowance from that year. The excess may also use up unused annual allowance from an earlier year. This can mean you may have to look back more than three years to work out how much of your allowance has been used. E.g. if you have exceeded £60,000 in 2024/25, this might be supported by unused allowance from as early as 2021/22, leaving unused allowance from 2022/23 and 2023/24 still available to carry forward to 2025/26.
- The annual allowance was £40,000 from 2016/17 to 2022/23.
- If you are subject to the money purchase annual allowance (see page 1) you will not be able to use carry forward to increase this.

You don't need to notify HM Revenue & Customs if you use carry forward to reduce or eliminate an annual allowance tax charge. We suggest you keep a copy of your calculations in case they are required.

This factsheet is not personal advice. Our financial advisers can help you pay less tax with careful financial planning. For complex tax calculations please speak to an accountant. Pensions can usually be accessed from age 55 (57 from 2028).



Hargreaves Lansdown  
One College Square South  
Anchor Road Bristol BS1 5HL

0117 980 9926  
pension.answers@hl.co.uk  
www.hl.co.uk

Issued by Hargreaves Lansdown Asset Management Ltd.  
Authorised & regulated by the Financial Conduct Authority.