

## **The Lifetime Allowance**

In the March 2023 Budget, announcements were made that will change the way the pension scheme is tested against the Lifetime Allowance. These changes are due to be brought in in April 2023 and April 2024.

Changes announced in the Finance (No.2) Act 2023 will make an adjustment to the tax position where lump sum payments over the available Lifetime Allowance are taken.

While it has been announced that the Lifetime Allowance will be removed from April 2024, HMRC has confirmed that all reporting requirements and tests against the Lifetime Allowance should continue for the 2023/2024 tax year.

The Lifetime Allowance (LTA) was introduced in 2006 and tests the value of all the pension benefits held by an individual. It includes the total of all the pensions held, including the value of pensions promised through any final salary schemes you may belong to, including any from which you may be receiving pension. It may also include any payment made from an employer in the event of death in service. It does not include state pension benefits.

The LTA applies to the value of your combined UK registered pension schemes and some overseas pension schemes. The value of your pension benefits can include any or all of the following:

- The value of any money purchase pension pots
- The value of any defined benefit plans. This will be calculated by the scheme and is usually 20 times the value of the pension – though some schemes are different and it is important you check this.
- The value of any pension plans in payment before April 2006 that have yet to be tested against the LTA. This is normally 25 times the pension in payment (certain conditions apply). This is only applicable if you take other benefits after April 2006.
- In the event of death, any payment from a registered group life scheme.

There is no limit on the value of pension savings that can be built up, but if it exceeds the LTA when the pension is taken, the amount in excess of the LTA will be subject to a tax charge known as the Lifetime Allowance charge. The Finance (No.2) Act 2023 has confirmed that for 2023/2024 the Lifetime Allowance charge will be 0%.

The LTA is expressed as a capital value and is set at a particular level each tax year. HM Treasury sets these limits, and they can increase/decrease them each year.

The standard LTA was frozen in the Finance (No.2) Act 2023, at £1,073,100. This also sets the limits for certain tax-free cash calculations.

## **How much is the LTA tax charge?**

The lifetime LTA tax charge is:

For 2023/2024 the Lifetime Allowance charge will be 0% but where a lump sum is paid from uncrystallised funds over the Lifetime Allowance, there will be tax charges on the beneficiary at their marginal rate of income tax\*.

## **What does it mean to test against the LTA?**

When you elect to draw benefits, you use up a proportion or percentage of your LTA. The circumstances where an LTA test occurs are called benefit crystallisation events (BCE). Each time you take new benefits, a capital value is given to the benefits that have been crystallised. This capital value is converted into a percentage of the LTA for the tax year in which the BCE occurred. That percentage is then measured or tested against your available LTA. A BCE may also occur on death or at age 75.

In the event of someone with pension benefits in payment prior to April 2006 taking benefits for the first time since 2006, the pension in payment is tested against the available LTA at the point of the first post-April 2006 BCE.

The percentage crystallised stays fixed, regardless of increases or decreases to the LTA.

## **Is the LTA the same for everyone?**

In some circumstances an individual's LTA will actually be higher than the Standard Lifetime Allowance (SLA) as set by HM Treasury. This can apply if you hold a certain type of pension credit or you are entitled to 'protection'.

There are rare circumstances where you would have a lower LTA than the SLA.

## **If protection gives you a higher LTA, why doesn't everyone have it?**

There are various forms of protection, including enhanced, primary, fixed and individual. However, there are certain restrictions that apply to having protection and certain protections were only available for a limited time.

If you have a protected LTA, you need to ensure your pension scheme providers are notified of your protected status to ensure it is not inadvertently invalidated.

The Finance (No.2) Act 2023 has removed some of these

restrictions from April 2023 making it possible for you to make contributions and still retain protection. The Finance (No.2) Act 2023 also sets limits on the amount of tax-free cash that can be taken dependant on the protected status of your pension schemes as at 15 March 2023.

## **Payments from a registered group life scheme**

Payments from a registered group life scheme do not have a value unless a payment is made. For some individuals, death benefits, if paid, can place them over the LTA.

From April 2023 changes announced in the Finance (No.2) Act 2023 will alter the way in which these benefits are paid if benefits are over the LTA. This will now be an income tax charge in the hands of the beneficiary where the benefits are paid as a lump sum.

If you have an existing pension you can retain existing membership of an existing group life scheme. Prior to 06 April 2023 if you joined a new group life scheme, or there was a change in the benefit structure of an existing group life scheme, this could have invalidated your protection. From 06 April 2023 if you had protection in place on 15 March 2023, joining a new group life scheme will not invalidate your protection.

## **Can I apply for protection?**

When the LTA was reduced in 2016, you were given the option to apply for either individual protection 2016 (IP16), which provided protection up to a maximum of £1.25 million (subject to your fund value being at least £1 million as of April 2016), or fixed protection 2016 (FP16), which provided protection of £1.25 million. There is no current deadline to apply for IP16 and FP16, but ideally your application should be made before benefits are taken.

Contributions can continue while you apply for IP16, but prior to 06 April 2023 if you are applying for FP16 you cannot have made any further contributions (or any benefit accrual) after 5 April 2016.

From 06 April 2023 making contributions will not invalidate existing protection. But if Fixed Protection 2016 is applied for after 06 April 2023, then making contributions after 06 April 2023 will invalidate the protection.

You can apply for IP16 and FP16 via <http://www.gov.uk/guidance/pension-schemes-protect-your-lifetime-allowance>. You will need a Government Gateway account to access this service. Unlike previous protections you will not receive a certificate, but a

reference number will be provided.

If you already have selected protection previously (enhanced, primary, fixed protection 2012, fixed protection 2014 or individual protection 2014) you will not be affected by these new protections and can retain your existing levels of protection (subject to conditions).

If you have enhanced or fixed protection, you can also apply for IP16, if you qualify.

For additional information on how to apply for the online protection, please contact your Mattioli Woods consultant.

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