

Reduction in the lifetime allowance

Guidance Notes

The information in this document is based on our interpretation of the relevant HM Revenue & Customs (HMRC) guidelines, which are subject to change. You should consult an FCA Registered Financial Adviser if you need help or advice on your specific circumstances.

Overview

The lifetime allowance is the maximum pension savings you can build up without a tax charge, over your lifetime. It is currently set at a level of £1.25 million but it is set to reduce to £1 million on 6th April 2016. Your pension benefits are tested against the lifetime allowance when you start to draw them from the scheme. This may be in one go or at different times depending on how you draw your benefits. Anything over the lifetime allowance will have a tax charge of either 25% if the residual money is left within the scheme to take as taxed income, or 55% if the money is taken out as a lump sum at the time of the test. If you do not draw your benefits before your death the value of them will be tested at that point, and a tax charge on any excess funds over the lifetime allowance may be chargeable to your beneficiaries.

When you draw benefits, only your pension commencement lump sum, usually 25% of the value of your fund up to the level of the lifetime allowance, will be tax free, the remainder will be drawn as an income which you will pay tax on in the same way as you would a salary (PAYE).

How will I know if I will be affected?

You will need to know the level of pension saving you have already accumulated, and this will depend on the type of pension scheme you have.

If you have a money purchase (defined contribution) pension scheme then it is simply the value of the fund including any pension commencement lump sum you are entitled to.

If you have a final salary (defined benefit) pension scheme then you need to know the amount of pension you would be paid assuming it were possible for you to take unreduced benefits on 5th April 2016. You then multiply this figure by 20 and add any pension commencement lump sum to the total.

If you have already started to receive benefits from a pension scheme these must also be taken into account, although the calculations will again differ depending on when you took the benefits and the type of benefits taken.

You may have many different schemes and the value of these will have to be aggregated for you to understand your overall pensions savings value for lifetime allowance purposes.

What protections will be available?

Fixed protection 2016

Fixed protection 2016 will give you a lifetime allowance of £1.25 million. There are no application restrictions for fixed protection 2016 in respect of the size of pension savings but it can be invalidated if:

- You have a contribution paid to any of your defined contribution pension schemes after 5th April 2016;
- You accrue further benefits in a defined benefit pension scheme above a certain amount after 5th April 2016;
- You join a new pension scheme after 5th April 2016 except to transfer your existing pension benefits to the scheme; or
- You start saving into a new pension arrangement either under one of your existing pension schemes or under a new pension scheme after 5th April 2016.

Should fixed protection be lost then the individual will revert to the standard lifetime allowance at that point in time, although any previous benefit crystallisations will not be recalculated to take account of the reduction.

Individual protection 2016

Individual protection gives a protected lifetime allowance equal to the value of pension rights on 5 April 2016 that exceed £1 million up to an overall maximum of £1.25 million. Calculations of the value of benefits an individual holds at 5th April 2016 are required to give an accurate protection value and this value will have to be stated on the application to HMRC for individual protection.

It is possible to continue to accrue benefits and make contributions with individual protection without losing the protection itself but any funds over the individual lifetime allowance will be subject to tax charges on crystallisation.

Individual protection can be held alongside fixed protection 2012, fixed protection 2014, fixed protection 2016 or enhanced protection, but not primary protection or individual protection 2014.

Individual protection 2014

Individual protection 2014 is basically the same as Individual protection 2016 but is available to those who had over £1.25 million at 5th April 2014 and protects up to a maximum of £1.5 million. It is still possible to apply for this form of protection, and the deadline for applying to HMRC is 5th April 2017

You will need to ask your pension provider(s) for valuation(s) as at 5th April 2014 to check if you are eligible and then complete the form online at <https://online.hmrc.gov.uk/shortforms/form/IP2014?dept-name=&sub-dept-name=&location=36&origin=http://www.hmrc.gov.uk> It is not possible to apply for individual protection 2014 if you already have primary protection (which you would have applied for between 2006 and 2009).

What should I do if I think this affects me?

You are currently unable to apply for fixed or individual protection 2016, the legislation is yet to be finalised. Applications should be available online from July 2016. Should you want to access benefits before then and rely on fixed or individual protection 2016, you should write to HMRC to gain interim protection. You will also then need to finalise the process when the applications become available. Details can be found here.

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

If you are intending to apply for fixed protection 2016 you must cease contributions, including employer contributions and cease accruing benefits in all pension schemes before 6th April 2016. If you do not then you will not be eligible to apply when applications become available.

Should you discover that your pension savings are already over £1.25 million there is still time to look into individual protection 2014, as stated above.

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