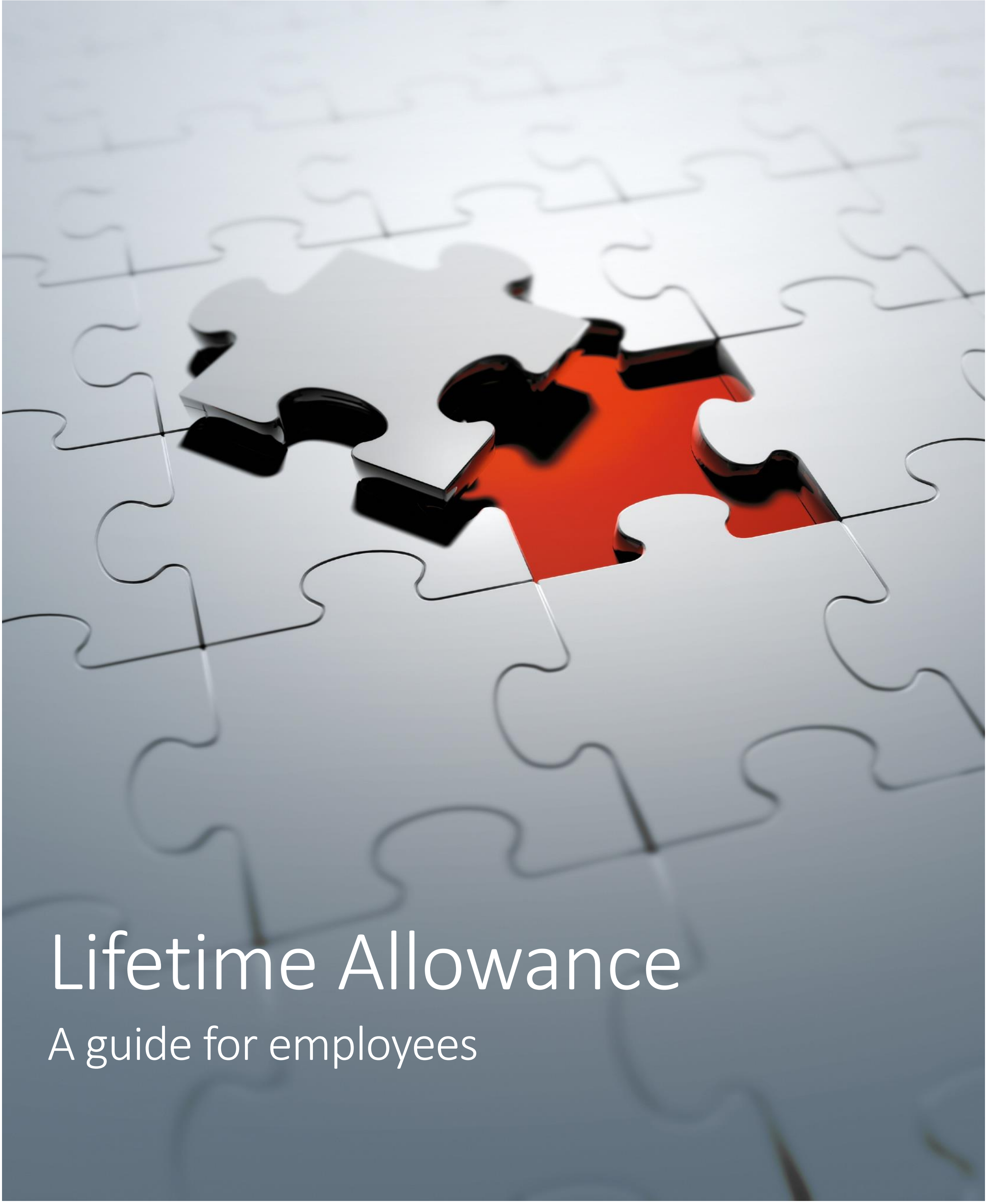

Lifetime Allowance

A guide for employees

one pension consultancy

Lifetime Allowance

This guide is aimed at employees to help them understand the Lifetime Allowance and identify if they may be impacted. Anyone who believes they may be impacted should seek independent financial advice.

This guide will consider the following issues:

1. What is the Lifetime Allowance and when is it tested?
2. How are benefits assessed against the Lifetime Allowance?
3. What happens if you exceed the Lifetime Allowance?
4. What happens if I die before taking my pension benefits?
5. What should I do if I am likely to exceed the Lifetime Allowance?

To help you consider whether or not you are likely to be affected by this, a summary of the rules is provided below. The rest of this booklet provides further detail and information around these points.

The Lifetime Allowance is the amount you can accrue from all your pension arrangements over your lifetime without tax consequences.

It is tested at certain events such as on taking benefits or death before drawing benefits.

The limit is currently £1 million (2017/18).

If your total pension funds exceed this limit you will be taxed on the excess. Usually this will be taxed at a rate of 55%.

If you die whilst an employee, the value of any lump sums payable from any Group Life Assurance or Death in Service Scheme benefit your employer provides will usually be added to your pension funds to test against this figure.

If you think you will be impacted you should seek advice.

What is the Lifetime Allowance?

The Lifetime Allowance is the maximum amount an individual can accrue under all their pension arrangements during their lifetime without incurring a tax charge. The Lifetime Allowance for the 2015/16 tax year was £1.25 million. However, this reduced to £1 million from April 2016. The Lifetime Allowance will remain at £1 million for the 2017/18 tax year. From the 2018/19 tax year it is expected that the Lifetime Allowance will be increased each year in line with the Consumer Prices Index (CPI) to help it maintain its real value going forward. However, the reduction in the Lifetime Allowance with effect from April 2016 will mean that more people are likely to be impacted by this in future.

The Lifetime Allowance was introduced in 2006. The table at the back of this booklet shows the history of the Lifetime Allowance for further information.

When is the Lifetime Allowance tested?

The Lifetime Allowance is tested at certain events, known as Benefit Crystallisation Events. The main ones are on drawing benefits from your pension arrangement or on death before drawing your pension if sooner. Some of the main Benefit Crystallisation Events are shown in the table below:

Event	Comments
You move your funds into Income Drawdown	The amount tested is the market value of the fund allocated to an Income Drawdown policy.
You become entitled to Scheme Pension	This is usually the pension you will receive from a Defined Benefit pension arrangement (such as a Final Salary pension). It can also apply to pensions from a Defined Contribution (or Money Purchase) arrangement such as a Group Personal Pension.
Your pension in payment is increased by more than a certain amount each year	This will apply to Defined Benefit pension arrangements (such as a Final Salary pension) where any annual increases awarded are greater than the higher of 5% or the increase in the Retail Prices Index.
You purchase an annuity	This is where you use a Defined Contribution (or Money Purchase) pension, such as a Group Personal Pension, to secure a fixed income payable for life.
You reach age 75 and have not drawn on your funds in your pension pot	This means that you still have money invested in your pension funds that hasn't been used to either purchase an annuity or assigned to Income Drawdown. A further test is also made against any undrawn funds under an Income Drawdown policy on your 75th birthday.
You take a lump sum from your pension	Under the new rules from April 2015 you will be able to access your pension as a lump sum. This will result in a test against the Lifetime Allowance.
If you die before drawing the benefits	If you die before drawing the benefits a lump sum may be payable. This will usually be the value of the fund (for Defined Contribution pensions such as Group Personal Pension) or a return of the personal contributions you have paid into the pension (for a Defined Benefit pension such as a Final Salary pension).
You transfer your pension pot to an overseas pension	If you transfer money to a Qualifying Recognised Overseas Pension Scheme this will be subject to a test against the Lifetime Allowance. If you transfer to an overseas pension that isn't qualifying and recognised, this will not be subject to the Lifetime Allowance but will be classed as an unauthorised payment which incurs significant tax charges. Transfers between UK pension arrangements are not subject to the Lifetime Allowance charge.

There are other events that will trigger a test against the Lifetime Allowance and if you are in any doubt as to whether or not you will be impacted you should seek advice.

How are benefits assessed against the Lifetime Allowance?

In most cases it is the fund value of any pensions you have that is tested against the Lifetime Allowance. An example of how this will work is shown below:

> Mark has two pension pots worth £450,000 in total which he uses to purchase an annuity in May 2017. He also has a pension fund of £750,000 which he puts into Income Drawdown at the same time. His total funds assessable against the Lifetime Allowance would be £1.2 million. The Lifetime Allowance in force in May 2017 is £1 million. His benefits will therefore be £200,000 in excess of the Allowance in force at that point in time.

How are Defined Benefit Pensions tested?

As any benefits from a Defined Benefit pension (such as, for example, a Final Salary pension) do not have a fund value as such, the pension payable is multiplied by a factor of 20 to test against the Lifetime Allowance. Any tax free lump sums are taken at face value. An example of this is shown below:

> In June 2017, Jane receives a pension from a final salary arrangement of £25,000 per annum. The amount tested against the Lifetime Allowance will be £500,000 (i.e. £25,000 x 20). She is also entitled to a tax free lump sum of £100,000 which brings the total amount to be tested against the Lifetime Allowance to £600,000. This is within the Lifetime Allowance in force at this date.

If I have several different pensions, what happens if I take them at different times?

If you take your benefits from different pension arrangements at different times, each time you draw on a pension you will use up a percentage of the Lifetime Allowance in force at that point in time. The example below shows how this may work:

> Steven takes one of his pension pots worth £125,000 in May 2015. At this point the Lifetime Allowance is £1.25 million. He therefore uses up 10% of the Lifetime Allowance. In May 2017 he draws on his remaining pension pots. These are tested against 90% of the Lifetime Allowance in force as at May 2017. The standard Lifetime Allowance in 2017 is £1 million. He will not face a tax charge unless his total funds are more than £900,000.

What about pensions in payment?

If you have any pensions already in payment, or if you have already entered into Income Drawdown for one or more of your pension arrangements, and these commenced after April 2006 you will have already used up a percentage of the Lifetime Allowance, as shown in the example above. You will have received correspondence from the pension provider which outlines the percentage of Lifetime Allowance you have already used. It is important that you keep this correspondence in a safe place as you will be asked to provide this information when you draw any further benefits from any pension arrangements (or else when you next reach a Benefit Crystallisation Event).

However, if your pension came into payment before April 2006, the rules are slightly different. If you have any pensions which came into payment before this date then the annual amount of pension in force as at the date a Benefit Crystallisation Event occurs (for example, the date you draw benefits from another pension arrangement) is multiplied by a factor of 25. This factor is higher than the factor used to test benefits from a Defined Benefit arrangement as it allows for the fact that a tax free lump sum was probably also taken when the pension was withdrawn. The below example shows how this may work:

Margaret started to receive a company pension worth £10,000 a year in December 2005. In July 2015 she draws on another pension with a fund value of £500,000, thus creating a Benefits Crystallisation Event. At this point the initial pension she was receiving has increased to £13,400 per annum. The amounts assessable against the Lifetime Allowance are as follows:

- £500,000 from her current pension fund
- £335,000 from her pension which commenced in 2005 (i.e. £13,400 x 25)
- This equals £835,000 in total which is below the Lifetime Allowance of £1.25 in force in July 2015.

What happens if I exceed the Lifetime Allowance?

If you exceed the Lifetime Allowance, a tax charge will apply to any benefit in excess of the Allowance in force. The excess can either be taken as a lump sum or used to provide an annual pension. The tax payable will depend upon how the excess is taken.

If the excess is taken as a lump sum this will be taxed at 55%. It should however be noted that it is only possible to take the excess as a lump sum if you are aged under 75. An example of this is shown below:

Chris is aged 65. He has total pension funds of £1.5 million when he comes to take his benefits in August 2016. He has exceeded the Lifetime Allowance in force at this point in time (£1 million for the 2016/17 tax year) by £500,000. He therefore pays tax of £275,000 if he takes this as a lump sum.

If the excess is taken as an annual pension, there will be an initial charge of 25% of the fund with the rest subject to Income Tax at the point the pension is paid. This means it will be taxable at either 20%, 40% or 45% dependent on your circumstances.

What happens if I die before drawing benefits?

As outlined above, death before drawing benefits is classed as Benefit Crystallisation Event and any lump sums payable will be tested against the Lifetime Allowance. You should bear in mind the following in this respect:

- Lump sums payable from a Defined Contribution arrangement, such as a Personal Pension or Stakeholder (including Group arrangements) are usually the fund value as at the date of death.
- Lump sums payable from a Defined Benefit arrangement, such as a Final Salary pension arrangement, are usually a return of the member contributions paid, with or without interest. This type of arrangement also usually pays out a spouse's or dependant's pension. These are not included within the figures to be assessed against the Lifetime Allowance but will be subject to Income Tax on the recipient.
- Any lump sums payable from your employer's Group Life Assurance or Death in Service arrangement will also be counted towards the Lifetime Allowance. Lump sums payable from other Life Assurance policies (such as term assurance or mortgage protection) are not counted towards the Lifetime Allowance. Any lump sums from an Excepted Group Life Assurance Scheme will also not count towards the limit.

In the event of your death, if the total amounts payable exceed the Lifetime Allowance in force, the excess will be subject to a 55% tax charge. Your personal representatives will be responsible for paying this to HM Revenue and Customs if this applies.

What should I do if I am likely to be impacted by the Lifetime Allowance?

If you are already over, or are very close to, the Lifetime Allowance you should seek advice on the best course of action. It may be that continuing to save in a pension arrangement is no longer the best thing for you to do but of course this will very much depend upon your circumstances.

Two forms of protection are available for anyone impacted by the reduction in the Lifetime Allowance from April 2016. More information on this can be found in the following:

http://onepc.co.uk/guides/fixed-and-individual-protection-2016/

History of the Lifetime Allowance

Tax year	Lifetime Allowance
2006/07	£1.5 million
2007/08	£1.6 million
2008/09	£1.65 million
2009/10	£1.75 million
2010/11	£1.8 million
2011/12	£1.8 million
2012/13	£1.5 million
2013/14	£1.5 million
2014/15	£1.25 million
2015/16	£1.25 million
2016/17	£1 million
2017/18	£1 million

The information contained in this document is based on One Pension Consultancy's understanding of the legislation as at June 2017. This document is for information purposes only and does not constitute advice.

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