

Avon Pension Fund

Local Government Pension Scheme

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Bath & North East
Somerset Council

for you, for now, for the future
lgps
2014



Pensions Taxation - Lifetime Allowance

HM Revenue and Customs impose two controls on the amount of pension savings you can make without having to pay extra tax. These controls are known as the annual allowance and lifetime allowance. This is in addition to any income tax you pay on your pension once it is in payment.

This factsheet looks at the Lifetime Allowance (LTA) which is the total value of all pension benefits you can have without triggering an excess benefits tax charge.

What is the lifetime allowance?

The lifetime allowance is the total value of all pension benefits you can have without triggering an excess benefits tax charge. If the value of your pension benefits when you take them (not including any state retirement pension, state pension credit or any partner's or dependant's pension you may be entitled to) is more than the lifetime allowance, or more than any protections you may have, you will have to pay tax on the excess benefits.

The lifetime allowance covers any pension benefits you may have in all tax-registered pension arrangements - not just the Local Government Pension Scheme (LGPS).

The lifetime allowance was introduced in 2006 and was reduced in 2012, 2014 and again in 2016. Each time the lifetime allowance reduced, if you had already planned your pension savings on the basis of the higher lifetime allowance you have been able to protect your pension savings by applying to HMRC for a lifetime allowance protection. These protections are covered in more detail later in this factsheet.

The lifetime allowance steadily reduced from 2012/13 to 2017/18. From 2018/19 onwards the lifetime allowance increases each year in line with inflation, see below:

Table 1 - the lifetime allowance from 2011/12

| Tax year | Lifetime allowance (£) |
|----------|------------------------|
| 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 | £1.00 million |
| 2017/18 | £1.00 million |
| 2018/19 | £1.03 million |
| 2019/20 | £1.055 million |
| 2020/21 | £1,073,100 million |

How is the lifetime allowance calculated?

For pensions that start to be taken on or after 6 April 2006, the capital value of those pension benefits is calculated by multiplying your annual pension by 20 and adding any lump sum you draw from the pension scheme.

Each time you take payment of a pension benefit the capital value of the benefits you are taking is expressed as percentage of the lifetime allowance limit applicable on that date and is deducted from your available lifetime allowance. So even if your pensions are small and individually will not be more than the lifetime allowance you should keep a record of any pensions you receive.

If you have a pension that came into payment before 6 April 2006, this will also be treated as having used up part of your lifetime allowance. For these pensions, the capital value is calculated by multiplying the current annual rate, including any pensions increase, by 25. Any lump sum already paid is ignored in the valuation.

When you take your LGPS benefits, if the capital value of those benefits is more than your available lifetime allowance you will have to pay tax on the excess. If your excess benefits are paid as a pension the tax charge will be 25% of the capital value of the excess; the ongoing pension payments be will also be subject to income tax. If the excess benefits are taken as a lump sum they will be taxed once only at 55%.

You can choose to pay the tax charge immediately by a reduction to your lump sum, pay the tax directly to HMRC yourself, or you can ask the scheme to pay the charge for you in return for a permanent reduction to your pension – this is called a lifetime allowance debit.

Examples

Sarah retires on 31 May 2020

| | |
|----------------------------------|-----------------|
| LGPS annual pension | £25,000 |
| LGPS lump sum | £45,000 |
| AVC taken as lump sum | £116,375 |
| Capital Value of benefits | £661,375 |

$(£25,000 \times 20) + £45,000 + £116,375$

Sarah has not taken any pension benefits previously.

The capital value of her benefits is less than the LTA for 2020/21 of £1,073,100.

She has used 61.63% of the available LTA.

Patrick retires on 31 May 2020

| | |
|----------------------------------|-------------------|
| LGPS annual pension | £50,000 |
| LGPS lump sum | £120,000 |
| Capital Value of benefits | £1,120,000 |

$(£50,000 \times 20) + £120,000$

Tax charge payable on benefits in excess of **£15,477 Tax charge**

£1,055,000 $(£65,000/20 \times 12 \times 55\%)$

Patrick has not taken payment of any pension benefits previously.

He has not applied for any lifetime allowance protection.

He has opted to be paid the benefits in excess of the LTA as a lump sum.

He has used 100% of the available LTA.

Changes to the lifetime allowance

The lifetime allowance reduced from £1.25 million to £1 million with effect from 6 April 2016. At that time two new protections were introduced called Fixed Protection 2016 and Individual Protection 2016. These protections are the same in design as Fixed and Individual Protections 2014 which were introduced when the lifetime allowance reduced from £1.5 million to £1.25 million in 2014.

Individual Protection 2016 (IP2016)

You can apply for IP2016 if your pension savings were valued at over £1 million (including pensions already in payment) on 5 April 2016. However, if you have primary protection you can't apply for IP2016.

IP2016 gives a protected lifetime allowance equal to the value of your pension rights on 5 April 2016 - up to a maximum of £1.25 million. You will not lose IP2016 by making further savings in to your pension scheme but any pension savings in excess of your protected lifetime allowance will be subject to a lifetime allowance charge.

Fixed Protection 2016 (FP2016)

You can apply for FP2016 if you expect your pension savings to be more than £1 million (including pensions already in payment) when you come to take them on or after 6 April 2016. FP2016 can be used to reduce or mitigate the lifetime allowance charge.

FP2016 is lost if your benefits increase by more than the cost of living increase in any one tax year. If you apply for and wish to keep FP2016 you must have opted out of the L G P S before 6 April 2016. The cost of living increase in 2016/17 was zero and thus any increase in your benefits on or after 6 April 2016 will result in the loss of FP2016.

FP2016 will also be lost if you start a new pension arrangement, other than to accept a transfer of existing pension rights, or if you pay contributions into a money purchase pension arrangement, other than to a life assurance policy providing death benefits that started before 6 April 2006. You will also be subject to restrictions on where and how you can transfer benefits.

You can't have FP2016 if you already have primary, enhanced, fixed protection 2012 or fixed protection 2014. With FP2016 your lifetime allowance is fixed at £1.25 million rather than the standard lifetime allowance.

If you lose FP2016 you must electronically notify HMRC within 90 days of the day on which you could first reasonably be expected to have known that you had lost this protection. Failure to do so could result in a fine of £300 and a penalty of up to £60 per day after the initial fine has been issued until you supply HMRC with the required notification.

Taking a tax-free lump sum

The maximum tax-free lump sum you can take on retirement is the lesser of:

- 25% of the capital value of your L G P S benefits, or
- 25% of the lifetime allowance which, for those with FP2016, is £312,500 (i.e. 25% of your lifetime allowance of £1.25million), or
- 25% of your remaining lifetime allowance if you have previously taken payment of (crystallised) pension benefits as you will have already used up some of your lifetime allowance.

Applying for Fixed and Individual Protection 2016

HMRC has introduced an online service for you to protect your pension lifetime allowance by applying for IP2016 or FP2016. <https://www.gov.uk/guidance/pension-schemes-protect-your-lifetime-allowance> There is no application deadline for IP2016 or FP2016. To apply for IP2016, you will need to inform HMRC of the value of your pension savings on 5 April 2016 and your pension administrator was only obliged to provide you with this information up to 5 April 2020. You must apply before you take your retirement benefits as you will need to provide the HMRC reference number to your pension administrator if you want to rely on the protection. Once you have successfully applied for protection, the online service will provide you with a reference number which you will need to keep.

Your pension savings may already be protected

The lifetime allowance was introduced in 2006 and was reduced in 2012, 2014 and again in 2016. Each

time the lifetime allowance reduced, if you had already planned your pension savings on the basis of the higher lifetime allowance you could protect your pension savings by applying to HMRC. If you have applied for a previous protection such as enhanced protection, primary protection, fixed protection 2012, individual protection 2014 or fixed protection 2014 you should have received a certificate to confirm your protection.

However you may still be subject to the lifetime allowance charge if you lose this protection.

You can find more information about Tax on your private pension contributions, these protections and when they may be lost on the Government's website <https://www.gov.uk/tax-on-your-private-pension/lifetime-allowance>

I think I might be affected – what should I do?

Before considering any action to reduce your tax liabilities you should always seek independent financial advice from an FCA registered adviser. For help in choosing an independent financial adviser visit the money advice website. <https://www.moneyadviceservice.org.uk/en/articles/choosing-a-financial-adviser>

There are certain considerations that you may wish to take into account:

- Converting annual pension for lump sum at retirement can reduce the capital value of your pension benefits
- If you wish to slow down your pension build up, the 50/50 section of the LGPS allows you to pay half your normal contributions and build up half your normal pension whilst still retaining full life and ill health cover
- If you opt out of the LGPS with the right to a deferred benefit you will not be able to aggregate your benefits if you re-join the LGPS.

If you have any questions about your L G P S membership or benefits, please contact Avon Pension Fund.

April 2020

This factsheet provides an overview of the LTA rules at April 2020. It should not be treated as a complete and authoritative statement of the law. The rules governing LTA can be complex and are subject to change; if you are unsure how to proceed you are advised to obtain independent financial advice.
