Firefighters' Pensions England
Scheme Advisory Board

Local Government Association

Information

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 (LTA) 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 draw them (not including any state retirement pension, 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 LTA covers any pension benefits you may have in all tax-registered pension arrangements - not just the Firefighters' Pension Schemes (FPS).

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 has been steadily reducing from 2012/13, but has been increased in line with inflation from 2018 onwards.

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	£1.0 million
2017/18	£1.0 million
2018/19	£1.03 million
2019/20	£1.055 million

How is the lifetime allowance calculated?

For pensions that start to be drawn 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.

For pensions already in payment before 6 April 2006, the capital value of these 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 any FPS benefit, or any other pension arrangement you may have, is put into payment you use up some of your lifetime allowance - so even if your pensions are small and individually will not be more than the LTA, you should keep a record of any pensions you receive. If you have a pension in payment before 6 April 2006, this will be treated as having used up part of your lifetime allowance.

If your FPS benefits are more than your lifetime allowance you will have to pay tax on the excess. If your excess benefits are paid as a pension the charge will be 25%, with income tax deducted on the ongoing pension payments; 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 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 of the lifetime allowance calculation are shown at Appendix 1.

Changes to the lifetime allowance

The lifetime allowance reduced from £1.25 million to £1 million with effect from 6 April 2016.

Two new protections have been introduced from 6 April 2016 and are known as Individual Protection 2016 and Fixed Protection 2016. These protections are the same in design as Individual and Fixed 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 Individual protection 2016 from 6 April 2016 if you have pension savings valued at over £1 million (including taking into account past benefits already in payment) on 5 April 2016. However, if you have primary protection or individual protection 2014 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 an overall 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 Fixed Protection 2016 from 6 April 2016 if you expect your pension savings to be more than £1 million (including taking into account past benefits already in payment) when you come to take them on or after 6 April 2016. FP2016 can be used to help reduce or mitigate the lifetime allowance charge.

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

• 25% of the capital value of your FPS benefits, or
• 25% of the lifetime allowance which, for those with fixed protection, 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

FP2016 is lost if your benefits increase by more than the cost of living increase. As the cost of living increase for the year 2016/17 was zero, any pension build up, however small, will lead to your pension increasing by more than zero. Therefore, if you applied for and wish to keep FP2016 you would have needed to have opted-out of the FPS with effect from 6 April 2016.

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.

If you lose fixed protection 2016 you must electronically notify HMRC within 90 days of the day on which you could first reasonably be expected to have known that an event had occurred causing you to have 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 them with the required notification.

Applying for Fixed and Individual Protection 2016

HMRC have introduced a new online self-service for pension scheme members to apply for individual protection 2016 (IP2016) or fixed protection 2016 (FP2016). There is no application deadline for IP2016 or FP2016, however, you must apply before you take your retirement benefits as you will need to provide the HMRC reference number to your pension fund administrator if you want to rely on the protection.

You will no longer receive a lifetime allowance protection certificate, instead once you have successfully applied for protection the online service will provide you with a reference number which you will need to keep.

An example of lifetime allowance protection is shown at Appendix 2.

Your pension savings may already be protected

As mentioned, the lifetime allowance was introduced in 2006 and was reduced in 2012, 2014 and again more recently 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 i.e. 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 these protections and when they may be lost at Tax on your private pension - lifetime allowance on the Government's website.

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.

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

- Converting annual pension for lump sum at retirement can reduce or increase the capital value of your pension benefits
- If you opt out of the FPS with the right to a deferred benefit you may not be able to draw this until later than you had expected

More information

If you have any questions about your FPS membership or benefits, please contact:

Firepensions@warwickshire.gov.uk

Disclaimer

This factsheet provides an overview of the lifetime allowance rules as at April 2019. 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. For help in choosing an independent financial advisor you can visit the money advice website.

Some of the examples shown in the appendix have been rounded to the nearest whole pound in order to simplify the calculations.

Appendix 1: example LTA calculations

Example 1

Simon retires on 30 June 2019 from FPS1992 with 30 years' service		
Final Pensionable Pay		£37,854
Pensionable Service	30 years, counting as	40/60ths
FPS Annual Pension before commutation	£37,854 x 40/60ths	£25,236 p.a.
FPS Annual Pension after commutation		£18,927 p.a.
FPS Lump Sum		£136,905
Capital Value of benefits (£18,927 x 20) + (£136,905)		**£515,445**
Simon has not drawn any pension benefits previously; the capital value of his benefits is less than the LTA for 2019/20 of £1,055 million. He has used 49% of the available LTA		

Example 2

Patricia retires on 31 August 2019 from FPS1992 with 30 years' service		
Final Pensionable Pay		£80,000
Pensionable Service	30 years, counting as	40/60ths
FPS Annual Pension before commutation	£80,000 x 40/60ths	£53,333 p.a.
FPS Annual Pension after commutation		£41,143 p.a.
FPS Lump Sum		£274,286
Capital Value of benefits (£41,143 x 20) + £274,286		**£1,097,146**
Tax Charge Payable on benefits in excess of £1.055m (£42,146 x 55%)		**£23,180**

This example assumes Patricia has not applied for any lifetime allowance protection and that she has opted to be paid the benefits in excess of the LTA as lump sum. She has used 100% of the available LTA.

Appendix 2: example of LTA protection

Sunil receives a forecast for retirement at age 55 on 6 October 2019 from FPS1992 with 30 years' service		
Final Pensionable Pay		£100,000
Pensionable Service	30 years, counting as	40/60ths
FPS Annual Pension before commutation	£98,000 x 40/60ths	£66,667 p.a.
FPS Annual Pension after commutation		£50,000p.a.
FPS Lump Sum maximum (25% of pension x commutation factor of 21.9 at age 55)		£365,000
Lifetime Allowance capital value of commuted pension benefits		**£1,365,000**

The capital value (for Lifetime Allowance) of Sunil's benefits after commutation would be £1,365,000 (£50,000 x 20 plus £365,000). As this is £310,000 above the current LTA a Lifetime Allowance tax charge would be due on this amount.

Sunil takes his estimate to a financial advisor. During their meeting, the advisor discovers Sunil had not previously applied for any LTA protection. The advisor recommends Sunil asks for an estimate of his pension benefits at 6 April 2016 to see if he can apply for Individual Protection 2016 in order to retain a protected lifetime allowance equal to the value of his pension rights at that time.

In order for Sunil to be eligible for IP2016, his benefits at 6 April 2016 must have been more than £1m. As he had not retired at that point, it is the pension **before** commutation built up at 6 April 2016 that must be used in the calculation.

Sunil's pension at 6 April 2016		
Final Pensionable Pay		£94,000
Pensionable Service	27.5 years, counting as	35/60ths
FPS Annual Pension before commutation	£94,000 x 35/60ths	£54,833 p.a.
Capital Value of benefits (£54,833 x 20)		**£1,096,660**

As Sunil's benefits were greater than £1m at 6 April 2016 before he retires he elects for IP2016 to protect his LTA at £1,096,660.

The maximum lump sum HMRC will allow without a tax charge is 25% of LTA. Any amount of lump sum which exceeds this is taxable at 55%.

Revised forecast with lump sum restricted to HMRC maximum		
Final Pensionable Pay		£100,000
Pensionable Service	30 years, counting as	40/60ths
FPS Annual Pension before commutation	£98,000 x 40/60ths	£66,667 p.a.
FPS Annual Pension after commutation		£54,148p.a.

HMRC Lump Sum maximum (25% of protected LTA)		£274,165
Lifetime Allowance capital value of commuted pension benefits		**£1,357,125**

The capital value of Sunil's benefits with IP2016 and reducing his lump sum to the maximum allowed by HMRC would be £1,357,125 (£54,148 x 20 plus £274,165). As this is £260,465 above his protected LTA a Lifetime Allowance tax charge would be due on this amount.

By applying for IP2016 and reducing his lump sum to the maximum allowed, Sunil has saved tax on nearly £50,000.