

Lifetime Allowance Employee Guide 2023/24

The Lifetime Allowance (LTA) will be fully abolished from the 2024/25 tax year, and the LTA tax charge will be removed for the 2023/24 tax year.

Summary

The LTA is a limit on the total amount of pension benefits you can build up in your lifetime before you need to pay an LTA tax charge. Testing against the LTA happens whenever benefits are taken from a pension, such as entering into drawdown, buying a lifetime annuity, taking a lump sum, on death and on reaching 75. These events are called Benefit Crystallisation Events (BCE).

The Government announced in the Spring Budget 2023 that the LTA will be fully abolished with effect from the 2024/25 tax year.

In the meantime the LTA tax charge will be removed for the 2023/24 tax year so that "nobody will face an LTA charge from April 2023". (Source: HMRC Pension Tax Limits Updated 17 March 2023)

What this means is that technically, for the 2023/24 tax year, the standard LTA remains in place at the same level as for 2022/23, which is £1,073,100. However for any BCE occurring after 6 April 2023 no LTA tax charge will arise. However, certain payments which would have been subject to an LTA tax charge will instead be taxed at the recipient's marginal rate of income tax.

The Autumn Statement 2023 confirmed that the Government will legislate in the Autumn Finance Bill 2023 to remove the LTA. In addition, the Bill will "clarify the taxation of lump sums and lump sum death benefits, and the application of protections" amongst other matters, and will take effect from 6 April 2024.

Tax-Free Cash

As a general rule, pension scheme members are able to take 25% of the money in their pension pot tax free. Given the LTA in 2022/23 was £1,073,100, the maximum amount of tax-free cash which could have been taken in that tax year was £268,275.

As part of the measures introduced in the Spring Budget 2023, the maximum amount of tax-free cash which may be taken in the 2023/24 tax year, and thereafter, has been frozen at £268,275. However, members with a protected right to a higher tax-free cash amount on 5 April 2023, will continue to be able to access this right.

LTA Protections

The LTA was first introduced on 6 April 2006 at £1,500,000. It increased every tax year thereafter until 6 April 2011, when it remained frozen at £1,800,000 for a second year. On 6 April 2012 it was reduced to £1,500,000 and further reductions took place from 6 April 2014 (to £1,250,000) and 6 April 2016 (to £1,000,000). Since 6 April 2018 it gradually increased to its current level of £1,073,100.

Each time the LTA was reduced, protections were made available by HMRC to pension scheme members to prevent those with significant existing pension benefits at that time from being penalised.

Different protections were made available as follows:

- Primary Protection
- Enhanced Protection
- Fixed Protection 2012
- Fixed Protection 2014
- Individual Protection 2014
- Fixed Protection 2016
- Individual Protection 2016

Each protection had certain requirements in order to qualify, and some had rules in order not to invalidate the protection in the future. For example, enhanced protection and fixed protection prevented members from being able to earn any future benefits in a HMRC registered pension scheme.

The purpose of each protection was to protect a defined amount of LTA and, in some cases, a defined amount of tax-free cash. For example, it was possible, under enhanced protection, to protect a tax-free cash sum greater than 25% of the fund.

Members had to apply to HMRC to receive a specific protection, and a certificate or reference number was given to the member by HMRC if they were successful.

Members can have more than one type of protection.

The Government confirmed in the Spring Budget 2023 that members who hold a valid enhanced protection or any valid fixed protections, will be able to accrue new pension benefits, join new arrangements or transfer from 6 April 2023 without losing this protection. HMRC confirmed that, for this to apply, the relevant protection must have been applied for before 15 March 2023, and a certificate or reference number subsequently issued.

Special rules apply to members who made a successful late application to HMRC for enhanced protection or fixed protection on or after 15 March 2023. Further details can be found in the HMRC Lifetime Allowance guidance newsletter - March 2023: <https://www.gov.uk/government/publications/lifetime-allowance-guidance-newsletter-march-2023>

Furthermore, as previously stated, the Government announced as part of the Autumn Statement 2023 that the Autumn Finance Bill 2023 will provide clarity on the application of protections, therefore we have more information to come. The LTA protections are complex and this document only provides an overview. If you were previously affected by the LTA, or have LTA protection from HMRC, you may wish to speak to an authorised financial adviser about the changes made in the budget. Further information can be found here: <https://www.gov.uk/guidance/pension-schemes-protect-your-lifetime-allowance>

Important Notices

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