

The pension lifetime allowance

A Technical guide

The pension lifetime allowance (LTA) was introduced as part of 'pension simplification' back on A-Day in April 2006. However, LTA planning can be far from straightforward given the constant changes made to the allowance over the years. In this guide, we examine some of the aspects of the lifetime allowance and how it can affect retirement planning.

Following the Chancellor's announcement in the Spring Budget, changes to the rules around the pension lifetime allowance start to come into effect from 6 April 2023. We've yet to receive final confirmation from HM Revenue & Customs (HMRC) on how these changes will be enacted and how they will affect our customers.

Contents

1. An introduction to the lifetime allowance	3
2. Transitional protection	4
2.1 Lifetime allowance protections	4
2.2 Primary protection (PP)	4
2.3 Enhanced protection (EP)	5
2.4 Fixed protection (FP)	5
2.5 Individual protection (IP)	6
2.6 Having more than one type of protection	7
3. LTA enhancements/reductions	7
3.1 Possible enhancements	7
3.2 Possible reductions	7
4. Benefit crystallisation events (LTA test trigger events)	8
5. Information requirements	13
5.1 Before the BCE	13
5.2 After the BCE	13

You can navigate the guide from the table of contents. Click on the segment you'd like to review and it'll take you directly to the page.

Important information

This document provides information and is only intended to provide an overview of the current law in this area and does not constitute financial advice, tax advice or legal advice, or provide any recommendations. Tax treatment depends on individual circumstances and all tax rules may change in the future. You cannot normally access your pension until age 55 (57 from 2028). Different options may have different effects for tax purposes, different implications for pension provision and different impacts on other assets and financial planning.

1. An introduction to the lifetime allowance

The lifetime allowance (LTA) was introduced in the 2006/07 tax year as part of 'pension simplification' (A-Day). It represents the total amount of pension benefits that an individual can build up over their lifetime that will enjoy full tax benefits. Any benefits taken in excess of the allowance will result in a tax charge of either 25% or 55% depending on how the benefit is taken (please see section 5 for more on the tax charge).

The allowance is set at £1.0731 million in the current tax year, although it has altered numerous times since it was initially introduced at £1.5 million in 2006. As the table below shows, the LTA reached a peak of £1.8 million in 2011 and steadily reduced up until 2016/17.

The standard lifetime allowance over the years

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
2018/19	£1.03 million
2019/20	£1.055 million
From 2020/21 to the current tax year	£1.0731 million

The LTA applies to both defined contribution (DC) and defined benefit (DB) pension schemes, with the benefits broadly valued in the following way (more information on valuations can be found in section 4):

- **Defined contribution schemes** – the value of the individual's pension savings (whether used to take an income or withdrawn as lump sums)
- **Defined benefits schemes** – usually 20 times the pension the individual receives in the first year plus any lump sum taken. So, for example, a final salary pension of £20,000 per annum will be valued at £400,000 (20 x £20,000) for the purposes of the LTA calculation.

Any entitlement to the UK State Pension has no impact on the LTA.

2. Transitional protection

With the introduction of the LTA in 2006, and at each time the allowance has been reduced, the government introduced protection measures to safeguard those people affected by the reduction. There are a number of regimes in place, which in essence gives the person applying for the protection their own personal LTA.

2.1 Lifetime allowance protections

Effective from	Protection type	Protection level	Continuing contributions?
April 2006	Primary	£1.8 million + enhancement factor (LAEF)	Yes**
April 2006	Enhanced	Unlimited	Please see the section below on enhanced protection
April 2012	Fixed 2012	£1.8 million	Yes**
April 2014	Fixed 2014	£1.5 million	Yes**
April 2014	Individual 2014	£1.25 million – £1.5 million	Yes**
April 2016	Fixed 2016*	£1.25 million	Yes**
April 2016	Individual 2016*	£1 – £1.25 million	Yes**

* Still available if qualification criteria met.

** Where protection was obtained before 15 March 2023 and contributions made from 6 April 2023.

2.2 Primary protection (PP)

Primary protection was introduced to protect people with pension savings of £1.5 million or more on 5 April 2006. It was also possible to include tax free cash entitlements within primary protection. It allows individuals to continue to make pension contributions after they have been granted protection. A person with this type of protection has a personal LTA (calculated when they take pension benefits), which is arrived at using a lifetime allowance enhancement factor (please see the box below).

Applications for primary protection were allowed until 5 April 2009. Once relied upon, it cannot be revoked and can only be lost in the event of a pension debit as a result of a pension sharing order following divorce.

Primary protection – calculating a personal LTA

A personal LTA is calculated using a lifetime allowance enhancement factor (LAEF), which is **added** to the standard LTA. This factor is calculated as follows:

$$(\text{Value of the individual's pension rights as at 5 April 2006} - \text{£1.5 million}) / \text{£1.5 million}$$

So, if someone had protected pension benefits of £3 million, their enhancement factor would be:

$$(\text{£3m} - \text{£1.5m}) / \text{£1.5m} = 1$$

The protection amount increased in line with changes to the standard lifetime allowance. When the LTA decreased to £1.5 million on 6 April 2012, individuals with primary protection retained a protected amount based on an underpinned LTA of £1.8 million. So, in the instance given above, the additional factor is 1 x £1.8 million, making a personal LTA of £3.6 million (£1.8m + £1.8m).

2.3 Enhanced protection (EP)

Anyone with certain pension rights as at 5 April 2006 could apply for enhanced protection, regardless of the value of their funds at that time (although any rights deemed excessive under occupational pension rules had to be surrendered). It was also possible to include tax free cash entitlements within enhanced protection. Any growth in the pension fund is also covered by the protection. Note that there are restrictions after 5 April 2023 in terms of this protection.

The attraction of this type of protection is that the individual is not tested against the lifetime allowance when they take benefits. However, enhanced protection will be lost in the following circumstances if they occurred before 6 April 2023:

- Where 'relevant benefit accrual' occurs under any arrangement in a registered pension scheme
- Where a transfer is made from any arrangement holding rights for the individual and that transfer is not a 'permitted transfer'
- Where a new arrangement is made for the individual other than to receive a permitted transfer, as part of a retirement-benefits activities compliance exercise, or as part of an age-equality compliance exercise
- Where an arrangement receives an impermissible transfer
- Where the member notifies HMRC that they no longer wish to be covered by enhanced protection.

It should be noted that auto-enrolment can cause the loss of enhanced protection (unless an employee opts out within one month or the employer chooses not to enrol such an employee in a scheme as they are not required to do so). Receiving a pension credit can also affect whether this type of protection is lost. Whether an individual can rebuild pension rights, which have been reduced following a pension debit, depends on the type of arrangement.

Applications for this type of protection were allowed until 5 April 2009.

2.4 Fixed protection (FP)

This new form of protection was introduced on 6 April 2012, following the reduction of the LTA to £1.5 million from £1.8 million. It provides a fixed level of allowance based on the LTA available prior to the reduction. As the LTA has been reduced on three occasions, three types of fixed protection have been made available:

- **Fixed protection 2012 (FP 2012)** – providing a LTA of £1.8 million (individuals wishing to rely on FP 2012 had to notify HMRC by 5 April 2012)
- **Fixed protection 2014 (FP 2014)** – providing a LTA of £1.5 million (individuals wishing to rely on FP 2014 had to notify HMRC by 5 April 2014)
- **Fixed protection 2016 (FP 2016)** – providing a LTA of £1.25 million (FP 2016 is still available – applying for this type of protection is covered in the box on the next page).

This type of protection will be lost if the protection was granted on or after 15 March 2023 and if the following conditions are not met:

- The individual cannot start a new arrangement other than to accept a transfer of existing pension rights
- The individual cannot have benefit accrual
- The individual is subject to restrictions on where and how they transfer benefits.

2.5 Individual protection (IP)

This type of protection (IP 2014) was introduced on 6 April 2014, following the reduction of the LTA to £1.25 million from £1.5 million. IP 2016 was made available from 6 April 2016, following the reduction of the standard LTA to £1 million.

Individual protection results in a personal LTA:

- **Individual protection 2014 (IP 2014)** – providing protection equal to the value of the person's pension rights on 5 April 2014 subject to a minimum of £1.25 million and capped at £1.5 million. Individuals wishing to rely on IP 2014 had to notify HMRC by 5 April 2017
- **Individual protection 2016 (IP 2016)** – providing protection equal to the value of the person's pension rights on 5 April 2016 (providing these were more than £1.0 million) and capped at £1.25 million. IP 2016 is still available – applying for this type of protection is covered in the box below.

To apply for this type of protection, an individual must calculate the value of their pension savings as they stood on 5 April 2014 (for IP 2014) or 5 April 2016 (for IP 2016). This valuation is the total of four amounts:

- **Amount A** – any pension that the member started to receive before 6 April 2006
- **Amount B** – any pension that came into payment after 5 April 2006 but before 6 April 2014 (for IP 2014) or 6 April 2016 (for IP 2016)
- **Amount C** – pension savings that the member has not yet taken from their registered pension scheme
- **Amount D** – pension savings that the member has not yet taken from certain overseas pension schemes.

Applying for IP 2016 or IP 2016

Clients can apply for protection online at the following address (they will need a Government Gateway user ID and password to use this service).

gov.uk/guidance/pension-schemes-protect-your-lifetime-allowance

There is no application deadline for these protections. However, to rely on the relevant protection, the client must have applied for and received a reference number from HMRC before their pension is tested against the LTA and they must have adhered to the relevant conditions. This applies even when the benefits being taken are worth less than the standard LTA.

2.6 Having more than one type of protection

It is possible for a client to have more than one type of protection, as indicated by the table below.

	PP	EP	FP 2012	FP 2014	FP 2016	IP 2014	IP 2016
PP	–	Yes	No	No	No	No	No
EP	Yes	–	No	No	No	Yes	Yes
FP 2012	No	No	–	No	No	Yes	Yes
FP 2014	No	No	No	–	No	Yes	Yes
FP 2016	No	No	No	No	–	Yes	Yes
IP 2014	No	Yes	Yes	Yes	Yes	–	No
IP 2016	No	Yes	Yes	Yes	Yes	No	–

Notes:

1. Enhanced protection takes precedence over primary and individual protections (i.e. the latter types are dormant)
2. Fixed protections take precedence over individual protections (i.e. the latter is dormant).

3. LTA enhancements/reductions

In addition to the transitional protections covered above, there are other situations where someone's LTA can be adjusted (subject to certain conditions). These are as follows:

3.1 Possible enhancements

1. Where a client transfers a recognised overseas pension to the UK which hasn't benefited from UK tax relief. For more information please refer to section [PTM095400](#) of the Pension Tax Manual on the government website.
2. If a 'disqualifying' pension credit is received following divorce, for benefits where payment started after A-Day, then an enhancement may be made, as the benefits have already been tested against the LTA. For more information please refer to section [PTM095200](#) of the Pension Tax Manual on the government website.
3. In limited circumstances and subject to certain conditions, a client with a UK-registered pension scheme may be able to apply for an enhancement where all or some of their benefits have accrued while they were a non-UK resident. For more information please refer to section [PTM095300](#) of the Pension Tax Manual on the government website.

It should be noted that whilst any enhancement can increase the overall LTA it does not change a client's pension commencement lump sum (PCLS) entitlement, this will remain as 25% of their LTA prior to the enhancement being applied.

3.2 Possible reductions

1. While any pension in payment prior to A-Day will never trigger a LTA tax charge in itself, the value of any pensions in payment are tested at the first benefit crystallisation event (these are listed in section 4) post A-Day, effectively reducing the available LTA. This reduction is covered in section 4 under 'Further notes related to BCEs'.
2. Any member with a protected retirement age of under 50 will have a reduced LTA if they take benefits before their normal minimum pension age (it is reduced by 2.5% for each complete year between the date on which the benefit crystallisation event occurs and the date on which the individual will reach normal minimum pension age).

4. Benefit crystallisation events (LTA test trigger events)

The legislation specifies the occasions when pension benefits must be tested against the lifetime allowance. If the member does not have sufficient LTA available, then a tax charge is likely to apply.

There are a number of scenarios which trigger a test and these are known as benefit crystallisation events (BCEs). There are 13 BCEs as shown in the table below. These generally only happen before or at age 75 (the exception is BCE 3 which can occur at any age).

LTA test trigger events	Valuation for BCE purposes	Tax charge (if LTA is exceeded)	Notes
BCE 1 Designating funds to drawdown during the member's lifetime (DC arrangements)	The value of funds (market value) placed into drawdown	0% from 6 April 2023	If the funds are subsequently used to purchase an annuity or to provide a scheme pension, an allowance is made for this as the funds have already been tested against the LTA (this is known as prevention of overlap).
BCE 2 When the person becomes entitled to a scheme pension before the age of 75 (whether a DB or DC arrangement)	Starting pension (the amount paid in the first 12 months) x 20 (the relevant valuation factor)	0% from 6 April 2023	<p>If entitlement to a scheme pension or lifetime annuity payments arises before normal minimum pension age, and the member does not satisfy the ill-health provision and does not have a protected pension age, a test will only be triggered under BCE 2 when the member reaches normal minimum pension age.</p> <p>If the scheme rules allow for a pension to increase by more than the permitted amount in a year (usually the greatest of 5%, RPI or £250), the member is likely to fall within the scope of BCE 3. To avoid this, a scheme administrator may approach HMRC to negotiate a relevant valuation factor (RVF) of more than 20.</p> <p>Where entitlement to a scheme pension arises from assets taken from a drawdown fund, an allowance is made for this as the funds have already been tested against the LTA (prevention of overlap).</p>

LTA test trigger events	Valuation for BCE purposes	Tax charge (if LTA is exceeded)	Notes
BCE 3 Where a scheme pension already in payment increases beyond a permitted margin	Value of increase above permitted maximum x 20 (RVF)	0% from 6 April 2023	<p>A test can be triggered when the annual increase is more than the greatest of RPI, 5% or £250.</p> <p>An increase can be greater than 5% if the scheme administrator has agreed with HMRC a relevant valuation factor (RVF) of more than 20.</p> <p>If the annual increase limit is exceeded, a second test against the 'permitted margin' will be conducted to determine whether BCE 3 will apply. More details on the permitted margin can be found in the Pension Tax Manual PTM088630 on the government website.</p> <p>Where a test has already been triggered through BCE 3, an allowance is made for this if the pension is increased again beyond the permitted margin (prevention of overlap).</p>
BCE 4 Purchase of a lifetime annuity from a DC arrangement before age 75	Value of the purchase (market value of funds), less the value of any amounts previously crystallised under BCE 1 if funds come from drawdown	0% from 6 April 2023	If a lifetime annuity is purchased before normal minimum pension age, and the member does not satisfy the ill-health provision and does not have a protected pension age, a test will only be triggered when the member reaches normal minimum pension age (the amount crystallises through BCE 2).
BCE 5 Uncrystallised defined benefits at age 75	Value of deferred scheme pension at 75th birthday x 20 (RVF) plus any lump sum not provided by commutation of pension	0% from 6 April 2023	If the scheme rules allow for a pension to increase by more than the permitted amount in a year (usually the greatest of 5%, RPI or £250), the member is likely to fall within the scope of BCE 3. To avoid this, a scheme administrator may approach HMRC to negotiate a relevant valuation factor (RVF) of more than 20.
BCE 5a Reaching age 75 while still in drawdown	Value of drawdown fund (market value) less the amounts previously crystallised under BCE 1	0% from 6 April 2023	A BCE 5a at age 75 is not triggered where the individual already had a drawdown fund in payment at A-Day (unlike drawdown that starts on or after A-Day which triggers a BCE 1 immediately and then a further BCE 5a at age 75 if there is any residual drawdown fund).

LTA test trigger events	Valuation for BCE purposes	Tax charge (if LTA is exceeded)	Notes
BCE 5b Reaching age 75 with uncrystallised money purchase funds	Value of the uncrystallised funds	0% from 6 April 2023	
BCE 5c A member dies before age 75 and uncrystallised funds are designated to beneficiary flexi-access drawdown (after 5 April 2015) within the relevant two-year period	Value of funds (market value) designated as available for drawdown	0% from 6 April 2023	The relevant two-year period starts on the date on which the scheme administrator first knew of the death or, if earlier, the day when they could first reasonably have been expected to know of it.
BCE 5d A member dies on or after 3 December 2014 and before age 75, and uncrystallised funds are used to purchase a beneficiary annuity (after 5 April 2015) within the relevant two-year period	Value of funds used to purchase annuity	0% from 6 April 2023	The relevant two-year period starts on the date on which the scheme administrator first knew of the death or, if earlier, the day when they could first reasonably have been expected to know of it.
BCE 6 Payment of a relevant lump sum before age 75 (other than on death): – Pension commencement lump sum (PCLS) – Serious ill health lump sum – Uncrystallised funds pension lump sum (UFPLS) – Lifetime allowance excess lump sum	Value of the relevant lump sum paid to the individual	Subject to PAYE income tax charge from 6 April 2023	The payment of an UFPLS is restricted to the amount of remaining LTA. If a larger lump sum is paid, the excess is treated as a lifetime allowance excess lump sum.

LTA test trigger events	Valuation for BCE purposes	Tax charge (if LTA is exceeded)	Notes
BCE 7 Payment of a lump sum death benefit, before age 75, from uncrystallised funds if paid within two years*	The value of the lump sum benefit	Subject to PAYE income tax charge from 6 April 2023	* The two-year condition only applies to uncrystallised funds lump sum death benefits paid after 5 April 2016.
BCE 8 Transfer to a qualifying recognised overseas pension scheme (QROPS) before age 75	Value of the transfer (market value), less any reduction for overlap	0% from 6 April 2023	Where a BCE 1 or a BCE 2 test has been previously applied, overlap provisions apply. Where an overseas transfer charge applies in respect of the transfer, the amount that is deemed to crystallise as a BCE 8 is the gross amount being transferred before the deduction of the overseas transfer charge.
BCE 9 Certain payments that constitute a prescribed event: <ul style="list-style-type: none"> – Payments of arrears of pension after death – Lump sums based on pension errors – PCLS-type lump sums paid after death 	Regulations will value and prescribe	Subject to PAYE income tax charge from 6 April 2023	

Further notes relating to BCEs

a) Pensions in payment on 5 April 2006

A pension in payment on 5 April 2006 (known as a pre-commencement pension) is only taken into account for LTA purposes when a BCE first occurs for a client (if no BCE ever occurs, then the pre-commencement pension will never be considered for LTA purposes).

When the first BCE occurs, the LTA available at that BCE will be reduced by the crystallised value of any pre-commencement pension in payment at that time, as valued immediately before that BCE. This is calculated by multiplying the annual rate of the pension in payment at the point of calculation, by a conversion factor of 25:1. No actual BCE occurs in respect of the pre-commencement pension and so no chargeable amount will ever be generated by it.

For more information on pension in payment calculations please refer to [PTM088300](#) of the Pension Tax Manual on the government website.

b) Where BCEs occur simultaneously

Normally, during the member's lifetime, BCEs use up the LTA in the chronological order in which they occur. The exception is where a pension commencement lump sum (PCLS) is paid and the BCE 6 test is conducted before the crystallisation of the associated BCE1, BCE 2 or BCE 4. Subject to this, the member must decide the order of the BCEs for the purpose of the LTA test. This is an important consideration if the client's LTA allowance is breached at this point, as the order determines which event creates the excess and is subject to the tax charge.

Where multiple BCEs occur as a result of death (BCE 5c, 5d and 7) although the BCE events may occur on different dates, for the purpose of calculating the LTA available, they are treated as occurring simultaneously immediately before the death of the member.

c) Phased retirement

Where a client draws an entitlement in stages, whether through fund designation in a DC scheme or through staggering a scheme pension or other benefit entitlement, each fresh entitlement is a separate BCE. So, if a client has a DC fund valued at £400,000 and they draw half of the fund at age 58 (e.g. £50,000 as a PCLS and £150,000 designated to drawdown), BCE 6 and BCE 1 occur at this time. If they draw the remaining fund in five years time, further BCEs will occur and a second LTA test will take place at that time.

d) BCEs and repayment of the overseas transfer charge

If a client makes a QROPS transfer that is subject to the overseas transfer charge, there are instances where this tax charge is repaid (broadly when it is paid in error or due to a change in circumstances). This repayment, which is made to the scheme administrator, must be used to provide benefits, or a transfer, in accordance with the scheme rules. If a BCE occurs in respect of these funds, an adjustment can be made to account for the fact that they have already been tested as a BCE 8.

Example of lifetime allowance and BCE calculation

December 2010	May 2015	May 2016	June 2018
Takes Pension Commencement Lump Sum of £200,000 and designates £600,000 to capped drawdown	Puts a defined benefit scheme into payment with an initial yearly income of £10,000 per annum	Applies for Fixed Protection 2016	Decides to purchase an annuity with their capped drawdown fund valued at £800,000
How much of the lifetime allowance has been used and therefore how much is remaining?			
PCLS triggers BCE 6 £200,000 of £1.8 million LTA = 11.11% used and 88.89% remaining	Scheme pension triggers BCE 2 (10,000 x 20) £200,000 of £1.25 million LTA = 16% used and 39.56% remaining		Annuity purchase triggers BCE 4 £800,000 - £600,000 (allowing for overlap) = £200,000 of £1.25 million LTA (based on Fixed Protection 2016 remaining in place) = 16% used and 23.56% remaining
Drawdown designation triggers BCE 1 £600,000 of £1.8 million LTA = 33.33% used and 55.56% remaining			

5. Information requirements

The LTA system is supported by an information exchange and reporting regime. There are different systems for reporting and paying the lifetime allowance charge depending on whether the BCE occurred during the member's lifetime or as a result of a BCE after the death of the member.

5.1 Before the BCE

If a member wants to rely on a form of LTA protection, they must give the scheme administrator the reference number issued by HMRC in connection with the relevant form of protection. If a member wants to rely on individual protection (IP 2014 or IP 2016), they must also give the scheme administrator details of the relevant protected amount.

5.2 After the BCE

Whenever a BCE occurs, the member must be given a statement telling them how much LTA has been used up by the event. This information will enable the member to work out if they have any LTA available at subsequent BCEs, and correctly complete any tax return. This requirement will fall either on the scheme administrator or an insurance company.

Where liability to the lifetime allowance charge arises, the scheme administrator must also give the member the following information:

- The chargeable amount that has arisen as a result of the BCE
- Details of how the chargeable amount has been calculated
- The amount of tax due
- Whether they have accounted for the tax, or intend to do so at a later date.

The scheme administrator must give the member a BCE statement:

- At least once every tax year if the member is receiving a pension from the scheme (this includes the member having designated funds to provide a drawdown pension), ending in the tax year in which the member reaches age 75
- Where they are not required to provide an annual BCE statement within three months of the BCE occurring (the exception is where they have to notify a deceased member's personal representatives).

More insights on tax and pensions

We're committed to providing you with technical support to help you keep pace with the latest rules and legislation. Our range of practitioner material is designed to help you keep on top of all aspects of retirement planning. Themes covered include death benefits, pensions and divorce, the State Pension, pension withdrawals taxation and much more.

Visit our Technical matters hub

fidelityadvisersolutions.co.uk/technicalmatters



Adviser Solutions

