



# Taxation of Pension Benefits Lifetime Allowance

## LIFETIME ALLOWANCE GUIDE (July 2012)

1. This Guide was originally published April 2011 and has now been updated to reflect changes LifeTime Allowance (LTA) policy.

### Purpose of LTA Guide

2. The purpose of this guide is to highlight the changes to LTA announced in the 2010 Budget to restrict pension tax relief. The LTA does not affect Armed Forces Compensation Scheme or Early Departure Payment. **Additionally, this guide only provides information based on the Armed Forces Pension Schemes; individuals with other pension arrangements must seek independent financial advice.** This guide should be read in conjunction with HMT/HMRC's latest guidance: [http://www.hm-treasury.gov.uk/consult\\_pensionsrelief.htm](http://www.hm-treasury.gov.uk/consult_pensionsrelief.htm)

### What is the LTA?

3. Since 6 Apr 06 no absolute limit has been placed on the amount of pension benefits an individual can receive from a single or amalgamation of, registered pension scheme(s). However, there is a maximum level of benefits (pension and /or lump sum) that can be drawn from all registered pension schemes without triggering certain tax charges; this maximum amount is called the Lifetime Allowance.

### What are the changes to the LTA?

4. The LTA has reduced from £1.8M to £1.5 million from financial year 2012/13. It is currently unknown if LTA will be increased beyond this date.

### When do I need to calculate whether I have exceeded the LTA?

5. Any event which results in payment of benefits (e.g. pension and /or lump sum) is known as a Benefit Crystallisation Event (BCE). When a BCE takes place the value of the pension plus lump sum will need to be tested against the individual's LTA. As an example, a BCE in the Armed Forces would be when leaving the Services and a pension and /or a lump sum is payable immediately.

### How do I know if I have exceeded the LTA at retirement?

6. The LTA calculation is the same for both AFPS 75 and AFPS 05; there are two parts to calculating whether you have exceeded the LTA:

- First, you must check whether your final Lump Sum, which is normally 3 x Annual Pension on retirement, is greater than  $\frac{1}{4}$  of the LTA ( $\frac{1}{4}$  of £1.5m is £375,000). If it is the excess is liable for tax.
- After calculating the lump sum, you must calculate the size of the pension pot. This is conducted by multiplying the amount of your Annual Pension on retirement by a factor of 20 and adding the Lump Sum (if it has not already been subject to tax in the first calculation).

**Example – no LTA tax liable**

An individual retires in Jul 12 with an annual pension of £40,000.

Lump Sum = £40,000 x 3 = £120,000

This is less than ¼ of £1.5M LTA (£375,000), therefore no tax is due on the Lump Sum and it must be included in the total pension pot calculation below.

Lump Sum = £40,000 x 3 = £120,000

Annual Pension x = £40,000 x 20 = £800,000

Factor = £800,000 + £120,000 = £920,000

Total pension pot value = £1,500,000

LTA for 2012/13

This is well within the LTA limit and therefore there is no tax liability.

7. The table below illustrates which rank, salary and pension amount are likely to attract a LTA charge. This is based on the assumption that this is the only pension provision and that the individual has served a full career.

Lifetime Allowance	Those likely to be affected by an LTA charge will have an annual pension (£PA) in excess of:	AFPS 75		AFPS 05	
		Likely to affect those on salary (£pa) in excess of:	Ranks likely to be affected:	Likely to affect those on salary (£pa) in excess of:	Ranks likely to be affected:
£1.5M	£65,217	£130K	OF 8 and above	£114K	OF7 and above

Note: Those on AFPS 05 could be affected at the rank of OF7 as AFPS 05 allows up to 40 years service to count towards the pension, whilst AFPS 75 allows up to 34 years.

**What happens if I breach the LTA?**

8. There is a LTA tax charge levied on the Lump Sum and/or the Annual Pension depending on the circumstances. Where the Lump Sum exceeds ¼ of the LTA of £1.5m (£375,000) the excess is taxed at 55% and recovered from the Lump Sum payment. Where the value of the pension pot exceeds the remaining available LTA the excess is taxed at 25%. This charge is then recovered from the Annual Pension using age related factors based on age at last birthday (appendix A) of the total charge for the life of the pension. Where LTA charges were incurred after 6 April 2012, upon payment, Widows/Widowers and Dependants pension benefits will be calculated on the unreduced pension. Where LTA charges were incurred prior to 6 April 2012, then these Dependants' benefits will be reduced.

**Example – no tax on Lump Sum but tax liable on pension pot**

A 58 year old female retires in Jul 12 with an annual pension of £70,000.

Lump Sum	= £70,000 x 3	= £210,000 <sup>2</sup>
Annual Pension x Factor	= £70,000 x 20	= £1,400,000
Total pension pot value	= £1,400,000 + £210,000	= £1,610,000
LTA for 2012/13		= £1,500,000
Excess over LTA		= £110,000
Taxed at 25%		= £27,500
Reduction in pension	= £27,500/20.41 <sup>1</sup>	= £1,347
New Annual Pension (for life)	= £70,000 - £1,347	= <b>£68,653</b>

9. However, if the Lump Sum exceeds a quarter of the LTA then the excess of the Lump Sum is taxed at 55% first as shown below – in practice this will happen on very few occasions.

**Example – tax liable on Lump Sum and pension pot**

A 61 year old male retires in Jul 12 with an annual pension of £130,000.

**Lump Sum Taxation @ 55%**

Lump Sum	= £130,000 x 3	= £390,000
A quarter of the LTA	= £1,500,000/4	= £375,000
Excess	= £390,000 - £375,000	= £15,000
Excess taxed at 55%		= £8,250
New Lump Sum	= £390,000 - £8,250	= <b>£381,750</b>

**Annual Pension Taxation @ 25%**

A second calculation must also be done to work out whether the annual pension element also exceeds the LTA. But, because the Lump Sum has now been taxed against £375,000 of the LTA, the second calculation must discount both the Lump Sum and the element of LTA it was assessed against in order to avoid taxing the same amount twice.

Therefore the remaining available LTA to test the pension value against is £1.125m (i.e. 3/4 of £1.5m).

Annual Pension x Factor	= £130,000 x 20 (note no lump sum)	= £2,600,000
Excess over £1,125,000	= £2,600,000 - £1,125,000	= £1,475,000
Excess taxed at 25%		= £368,750
Reduction in pension	= £368,750/18.14 <sup>3</sup>	= £20,328
New Annual Pension (for life)	= £130,000 - £20,328	= <b>£109,672</b>

<sup>1</sup> Taken from column 1 Table E2: Pensioner Lifetime Allowance Factor table – 58 year old female.

<sup>2</sup> Not greater than ¼ of £1.5 million LTA (£375,000) therefore there is no tax charge on the Lump Sum.

<sup>3</sup> Taken from column 1 Table E1: Pensioner Lifetime Allowance factor table – 61 year old male.

## LTA PROTECTION

### Primary Protection and Enhanced Protection

10. There are already two forms of LTA protection in existence; Primary Protection and Enhanced Protection which were open to individuals until 5 Apr 09. Individuals already covered by these types of protection will continue to be unaffected by the reduction in the LTA. Individuals holding protection may still incur a tax charge if they breach the terms of their protection. Further Details can be found at <http://www.hmrc.gov.uk/manuals/rpsmmanual/rpsm03201000.htm>

### Fixed Protection

11. A new form of protection called Fixed Protection was introduced (August 2011) which gave individuals the opportunity to fix their LTA at £1.8m rather than the new LTA of £1.5m. Members had to stop building up benefits under every registered scheme of which they were a member by 5 Apr 12. For members of the Armed Forces pension Scheme(s) members had to inform SPVA on their decision to elect Fixed Protection by 31<sup>st</sup> March 2012. This means that the value of the pension as at 31<sup>st</sup> March is effectively frozen until retirement, and members cannot join any subsequent scheme on leaving the Services or they will lose Fixed Protection and may face a tax charge. In these circumstances, regardless of pay increases or promotion, the pension will only grow thereafter in accordance with the current indexation rate (currently the CPI). Individuals holding Fixed Protection may still incur a tax charge if they exceed the £1.8M LTA limit.

12. Individuals who continued to hold Primary or Enhanced Protection were not eligible to apply for Fixed Protection.

13. Members holding Fixed, Primary or Enhanced Protection may also be affected by the use of age related factors to recover LTA tax charges if any of their benefits are subject to a Lifetime Allowance charge under the rules of their protection.

## **Appendix A**

**Armed Forces Pension Scheme  
Pension Sharing on Divorce Factors for establishing the  
reduction in members pensions through exceeding the LTA  
– applicable from 06 April 2012**

### **How to use the factor tables:**

1. To calculate the factor by which the pension will be reduced the member needs to identify the correct table.
2. Tables:
  - a. E1 – Retirement not on grounds of ill health Males;
  - b. E2 - Retirement not on grounds of ill health Females;
  - c. F1 – Retirement on grounds of ill health Males;
  - d. F2 - Retirement on grounds of ill health Females.
3. Members should use Column 1, referring to the age at their last birthday.
4. Once the factor has been established the tax charge should be divided by this factor to establish the yearly reduction.

**Table E1: Pensioner Lifetime Allowance Factor Table**

**Retirement *not* on grounds of ill health – Males**

<b>Age last birthday at relevant date</b>	<b>Gross Pension of £1 per annum</b>
16	24.27
17	24.31
18	24.34
19	24.38
20	24.41
21	24.43
22	24.46
23	24.48
24	24.49
25	24.50
26	24.51
27	24.51
28	24.51
29	24.51
30	24.49
31	24.47
32	24.45
33	24.42
34	24.38
35	24.34
36	24.28
37	24.22
38	24.15
39	24.07
40	23.97
41	23.87
42	23.75
43	23.62
44	23.47
45	23.31
46	23.13
47	22.93
48	22.71
49	22.48
50	22.22
51	21.93
52	21.63
53	21.30
54	20.95
55	20.57
56	20.18
57	19.79
58	19.38
59	18.97
60	18.56
61	18.14
62	17.71
63	17.27
64	16.83



**Table E1: Pensioner Lifetime Allowance Factor Table**

**Retirement *not* on grounds of ill health – Males (*continued*)**

**Age last birthday at relevant date      Gross Pension of £1 per annum**

65	16.37
66	15.90
67	15.43
68	14.94
69	14.44
70	13.94
71	13.45
72	12.95
73	12.45
74	11.95
75	11.45
76	10.95
77	10.44
78	9.93
79	9.42
80	8.90
81	8.39
82	7.89
83	7.40
84	6.93
85	6.49
86	6.07
87	5.67
88	5.30
89	4.96
90	4.64
91	4.35
92	4.08
93	3.82
94	3.58
95	3.35
96	3.11
97	2.89
98	2.67
99	2.47
100	2.29

## Table E2: Pensioner Lifetime Allowance Factor Table

### Retirement *not* on grounds of ill health – Females

Age last birthday at relevant date      Gross Pension of £1 per annum

16	24.58
17	24.62
18	24.67
19	24.71
20	24.75
21	24.79
22	24.82
23	24.85
24	24.88
25	24.91
26	24.92
27	24.94
28	24.95
29	24.96
30	24.96
31	24.95
32	24.94
33	24.92
34	24.89
35	24.86
36	24.82
37	24.77
38	24.71
39	24.64
40	24.56
41	24.46
42	24.36
43	24.24
44	24.11
45	23.97
46	23.81
47	23.63
48	23.43
49	23.22
50	22.99
51	22.73
52	22.46
53	22.16
54	21.84
55	21.50
56	21.14
57	20.78
58	20.41
59	20.03
60	19.64
61	19.24
62	18.83
63	18.41
64	17.98

**Table E2: Pensioner Lifetime Allowance Factor Table**

**Retirement *not* on grounds of ill health – Females (*continued*)**

<b>Age last birthday at relevant date</b>	<b>Gross Pension of £1 per annum</b>
65	17.54
66	17.09
67	16.63
68	16.16
69	15.68
70	15.19
71	14.70
72	14.20
73	13.69
74	13.18
75	12.67
76	12.15
77	11.62
78	11.09
79	10.55
80	10.00
81	9.46
82	8.92
83	8.39
84	7.89
85	7.40
86	6.94
87	6.50
88	6.09
89	5.69
90	5.32
91	4.97
92	4.63
93	4.31
94	4.01
95	3.72
96	3.44
97	3.18
98	2.94
99	2.72
100	2.52

## Table A1: Pensioner Lifetime Allowance Factor Table

### Retirement on grounds of ill health – Males

Age last birthday at relevant date      Gross Pension of £1 per annum

16	29.15
17	28.99
18	28.83
19	28.67
20	28.50
21	28.33
22	28.15
23	27.97
24	27.78
25	27.59
26	27.39
27	27.19
28	26.98
29	26.76
30	26.55
31	26.32
32	26.09
33	25.85
34	25.61
35	25.36
36	25.10
37	24.83
38	24.56
39	24.27
40	23.98
41	23.68
42	23.37
43	23.06
44	22.73
45	22.39
46	22.04
47	21.69
48	21.32
49	20.95
50	20.57
51	20.18
52	19.79
53	19.38
54	18.97
55	18.56
56	18.14
57	17.71
58	17.27
59	16.83
60	16.37
61	15.90
62	15.43
63	14.94
64	14.44

**Table F1: Pensioner Lifetime Allowance Factor Table**

**Retirement on grounds of ill health – Males (*continued*)**

<b>Age last birthday at relevant date</b>	<b>Gross Pension of £1 per annum</b>
65	13.94
66	13.45
67	12.95
68	12.45
69	11.95
70	11.45
71	10.95
72	10.44
73	9.93
74	9.42
75	8.90
76	8.39
77	7.89
78	7.40
79	6.93
80	6.49
81	6.07
82	5.67
83	5.30
84	4.96
85	4.64
86	4.35
87	4.08
88	3.82
89	3.58
90	3.35
91	3.11
92	2.89
93	2.67
94	2.47
95	2.29
96	2.12
97	1.97
98	1.83
99	1.71
100	1.61

## Table F2: Pensioner Lifetime Allowance Factor Table

### Retirement on grounds of ill health – Females

Age last birthday at relevant date	Gross Pension of £1 per annum
16	29.52
17	29.37
18	29.22
19	29.07
20	28.91
21	28.75
22	28.59
23	28.42
24	28.24
25	28.06
26	27.87
27	27.68
28	27.49
29	27.28
30	27.07
31	26.86
32	26.64
33	26.41
34	26.18
35	25.94
36	25.69
37	25.44
38	25.18
39	24.92
40	24.64
41	24.36
42	24.07
43	23.78
44	23.47
45	23.16
46	22.84
47	22.52
48	22.18
49	21.84
50	21.50
51	21.14
52	20.78
53	20.41
54	20.03
55	19.64
56	19.24
57	18.83
58	18.41
59	17.98
60	17.54
61	17.09
62	16.63
63	16.16
64	15.68

## Table F2: Pensioner Lifetime Allowance Factor Table

### Retirement on grounds of ill health – Females (*continued*)

Age last birthday at relevant date	Gross Pension of £1 per annum
65	15.19
66	14.70
67	14.20
68	13.69
69	13.18
70	12.67
71	12.15
72	11.62
73	11.09
74	10.55
75	10.00
76	9.46
77	8.92
78	8.39
79	7.89
80	7.40
81	6.94
82	6.50
83	6.09
84	5.69
85	5.32
86	4.97
87	4.63
88	4.31
89	4.01
90	3.72
91	3.44
92	3.18
93	2.94
94	2.72
95	2.52
96	2.34
97	2.17
98	2.01
99	1.88
100	1.77