

GUIDE TO THE ABOLITION OF THE LIFETIME ALLOWANCE



What is changing on 6 April 2024?

On 6 April 2023, the lifetime allowance charge was removed. The lifetime allowance tests continued after this date. On 6 April 2024, the lifetime allowance itself is being removed. This does not mean however that the amount of tax-free income which can be taken is now unlimited. There are new allowances being introduced to replace the outgoing lifetime allowance.

What is replacing the lifetime allowance?

Three new allowances are being introduced.

- The lump sum allowance (LSA) - £268,275
- The lump sum and death benefit allowance (LSDBA) - £1,073,100

Both allowances limit the amount of tax-free benefits which can be paid, but importantly, only apply to lump sums.

There is also a third allowance.

- The overseas transfer allowance - £1,073,100

These limits may be higher if the individual has lifetime allowance protection.

Anything else which is new?

A new authorised lump sum is being introduced, the “pension commencement excess lump sum (PCELS)”. It is payable, where the scheme rules allow, when none of the individual’s lump sum allowance or none of the individual’s lump sum and death benefit allowance is available. It enables individuals to continue to receive a lump at retirement, after they have exhausted one, or both of the new allowances.

Goodbye to BCEs

Benefit Crystallisation Events (BCEs) have all been removed and in their place, we have the “Relevant Benefit Crystallisation Event” (RBCE).

So, what is a Relevant Benefit Crystallisation Event (RBCE)?

Despite using similar words, the relevant benefit crystallisation event (RBCE) is very different to the old benefit crystallisation event (BCE). The RBCE refers only to the tax-free element of the benefits being taken. There are no relevant benefit crystallisation events for taxable income. This means that RBCEs are only triggered in a limited number of scenarios. For example, an uncrystallised fund pension lump sum payment, a serious ill health lump sum, a pension commencement lump sum and a lump sum death benefit payment.

What are the BCEs?

The new RBCEs are:

- RBCE 1 – Drawdown
- RBCE 2 – Scheme Pension
- RBCE 3 – Scheme Pension Increases
- RBCE 4 – Lifetime Annuity
- RBCE 6 – Lump sums – PCLS, standalone lump sums, UFPLS

So, the only ones relevant to IFGL Pensions will be RBCE 1 and RBCE 6

When is the Lump Sum Allowance assessed?

The LSA is assessed when a RBCE is triggered by the following:

- A pension commencement lump sum (PCLS)
- An uncrystallised funds pension lump sum (UFPLS)

The lump sum allowance is reduced by the amount of PCLS or in the case of the UFPLS, the tax-free element.

When is the Lump Sum and Death Benefit Allowance assessed?

The LSDBA is assessed when a RBCE is triggered by the following:

- A pension commencement lump sum (PCLS)
- A serious ill health lump sum (SIHLS)
- An uncrystallised funds pension lump sum (UFPLS)
- An authorised lump sum death benefit other than a charity lump sum death benefit, or trivial commutation lump sum death benefit, including both uncrystallised fund lump sum death benefits and drawdown pension lump sum death benefits and flexi-access drawdown lump sum death benefit payments paid after 6 April 2024.
- Pension protection lump sum death benefit payment
- Annuity protection lump sum death benefit payment

How is the Overseas Transfer Allowance (OTA) assessed?

Any transfer to a QROPS is assessed against the OTA (£1,073,100). The excess is charged at 25%. In addition, the OTA is reduced by any LTA usage which has taken place prior to 6 April 2024. The existing Overseas Transfer Charge (OTC) rules and exemptions still apply and where it is charged, the OTC interacts with the OTA charge.

What about benefits taken before 6 April 2024?

Where someone has previously used 100% or more of their lifetime allowance, there will be no entitlement to either the LSA or LSDBA. Where less than 100% of the lifetime allowance was used before 6 April 2024, both the LSA and LSDBA will be reduced by 25% of the percentage of the lifetime allowance which was used.

Example. Bill crystallised £1,200,000 in May 2012, when the lifetime allowance was £1,500,00. He therefore used 80% of the LTA. His LSDBA will therefore be reduced by 0.25 of this 80% figure = £214,620, leaving him with £858,480". His LSA will be reduced by 25% of the 80% figure too, so £268,275 - (£214,620) = £53,655.



What tax is paid when the LSA or LSDBA allowances are exceeded?

Benefits which exceed the new allowances will be liable to income tax at the recipient's marginal tax rate. So, for example, if an individual has income of £55,000 in a tax year and receives an excess of £15,000, it will all be charged at 40% because their income is in the higher rate band.

What is a transitional tax-free cash sum certificate?

This is a certificate which is provided on application to the scheme. It shows the individual's transitional tax-free cash amount and the individual's lump sum and lump sum and death benefit transitional tax-free amount. It is relevant where someone has taken benefits before 6 April 2024, but not received the full 25% tax-free cash amount, in which case the standard LSA and LSDBA calculations might not be appropriate for them. It might also be preferable for someone who crystallised benefits when the lifetime allowance was only £1,000,000. HMRC expects that the request for a certificate will go to the scheme who will pay the first benefits after 6 April 2024.

Are there any benefits not tested against the new allowances?

- Small lump sum payments (small pots) of under £10,000 are not tested against either of the new allowances.
- A winding-up lump sum.
- A trivial commutation lump sum.
- A charity lump sum death benefit.
- A trivial commutation lump sum death benefit.

Can you still apply for Fixed Protection 2016 or Individual Protection 2016?

Yes, applications for these protections, which give an enhanced allowance, can still be made, but only up to 5 April 2025.