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ALL MATTERS FINANCIAL

CHANGES TO THE LIFETIME ALLOWANCE & ANNUAL ALLOWANCES

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In the Budget on 15 March 2023, the Government announced several changes to the annual allowance, lifetime allowance and tax-free cash. This was followed by the Finance (No.2) Bill 2023 which once it becomes an Act will put some of these changes into legislation from 6 April 2023. Other changes announced in the Budget will not take effect until the 2024/25 tax year, and further information is expected on these later in the year.

Key facts

- Annual allowance is now £60,000.
- Money purchase annual allowance is now £10,000.
- There will be no lifetime allowance charge in tax year 2023/24.
- The lifetime allowance will be abolished from 6 April 2024.
- Maximum tax-free cash will be frozen at £268,275 from 6 April 2024.

THE ABOLITION OF THE LIFETIME ALLOWANCE

Britons can now expect significant changes that will affect their retirement savings. The changes are designed to alleviate the impact of strict pension rules, which are believed by Mr Hunt to have had a negative impact on the country's labour market.

Exceeding the allowance

The most significant change was the abolition of the pension Lifetime Allowance (LTA) charge. As of 6 April 2023, the LTA charge for registered pension schemes has been completely removed, with total abolition set for April 2024.

The LTA is the maximum amount of savings an individual can make in a registered pension scheme without incurring a tax penalty.

The standard LTA for the 2022/23 tax year was set at £1,073,100, which meant those with pensions exceeding this amount would face a tax charge.

However, with the abolition of the LTA charge, individuals can now contribute as much as they like to their pension schemes without fear of being penalised for exceeding the allowance.

This is particularly good news for those with pensions of significant value, as they will no longer be forced to limit their contributions to avoid a tax charge.

If you paused pension contributions because you were concerned you might breach the LTA, you may decide you want to make further tax-efficient additions to your pot. It is also worth noting that the government tax relief on pension contributions will still be available, which means individuals can continue to benefit from this incentive.

Tax-free lump sum

Additionally, under the previous pension rules, an individual could withdraw up to 25% of their pension savings as a tax-free lump sum, but that has now changed. The tax-free lump sum that can be normally drawn at age 55 (rising to 57 from 6 April 2028) is now capped at £268,275, and it is expected that another cap will be set in 2024 once the LTA is fully abolished.

This means that those who have saved a large amount in their pension may not be able to withdraw as much as they had planned. To ensure that your retirement plans are not affected by these changes, it is essential to obtain professional financial advice and discuss what is the best course of action for your situation.

UK'S pension system

The removal of the LTA marks a significant change to the UK's pension system, and it remains to be seen how this will impact pension savings and retirement planning in the years to come.

The tax-relievable annual pension contribution limit has also increased from £40,000 to £60,000, which is good news for most people. The annual allowance might be lower for those who have flexibly accessed their pension pot and for high earners.

Attractive investment option

Pensions have always been an attractive investment option with tax-relievable contributions, tax-free returns, and usually no Inheritance Tax. The removal of the LTA tax regime and the opportunity to rebuild pension benefits with an increased allowance are excellent news for many pension savers.

ANNUAL ALLOWANCE INCREASED TO £60,0000

When making contributions to your pension, it's important to keep in mind that there's a limit to how much you can contribute each year without incurring additional taxes.

This limit is known as the pension Annual Allowance.

On 6 April 2023, new pension legislation came into effect, presenting significant opportunities for various individuals. Among other things, the pension Annual Allowance increased from £40,000 to £60,000.

Additionally, the 'adjusted income' threshold for Annual Allowance tapering increased from £240,000 to £260,000 and the minimum tapered Annual Allowance increased from £4,000 to £10,000 (meaning that individuals with annual adjusted income of £360,000 or more will have an Annual Allowance of £10,000).

Excess contributions

If you exceed the Annual Allowance, you won't receive tax relief on the excess contributions, and you may be subject to an Annual Allowance charge. One way to reduce or eliminate this charge is by taking advantage of carry forward.

This option allows you to use any unused allowance from the previous three tax years to increase your contribution in the current year, subject to certain conditions. However, you need to have sufficient earnings to permit the size of contribution.

Carry forward is not available to everyone, it's only available to those who are not subject to the Money Purchase Annual Allowance (MPAA).

Additionally, you'll need to make sure that you don't exceed your Net Relevant Earnings in the current tax year, even after using carry forward.

Tax benefits

If you do find yourself facing a pension Annual Allowance charge, you may be able to ask your pension scheme to pay the charge from your pension using Scheme Pays.

This would result in a reduction in your pension, so it's important to carefully consider whether this is the right option for you.

It's important to recognise the tax benefits associated with contributing to your pension plan and staying up to date on changes to pension allowances and contribution rules.

Given the tax benefits associated with contributing to a pension plan, it's worth considering whether increasing contributions can help you meet your long-term retirement savings goals.

FURTHER INFORMATION

It is important to note that the abolition of the LTA has not yet been turned into legislation and may still be subject to change.

The government has stated that it will consult on the proposal before making a final decision.

You can find the detailed proposed legislation for these changes in the Finance Bill.

HMRC will also continue to give updates via their Pension schemes newsletters as information becomes available.

As always, if you have any questions or concerns please contact your adviser to discuss.

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