Annual Allowance Quick Guide

SCOTTISH PUBLIC PENSIONS AGENCY

CARE about your future

Are you facing a tax bill?

From 6 April 2016, there was significant changes to the allowances for tax efficient pension savings, which could result in you paying an additional tax on your scheme benefits when you retire.

In the past, these allowances have mainly affected senior officials and those on a progressive career path with frequent promotions. However, we now expect more members to be restricted by these allowances, particularly those with longer periods of service or members who are now earning benefits at double the standard rate (some police officers, firefighters and mental health officers).

In this factsheet, we explain how you might be affected and what you need to do. It's important that you read and understand the impact this may have on you and your retirement, particularly if at least one of these applies to you:

- you have recently been promoted.
- you have been awarded a pay rise.
- you have a long period of service.
- you are earning benefits at double the standard rate.
- you earn more than £100,000 a year.

Why is this so important?

Scheme membership offers you a tax-efficient way to save for your retirement. You receive tax relief on your contributions and you can take a tax-free lump sum when you retire. HMRC sets limits on how much you can benefit from these efficiencies and does this by giving you two allowances:

1. **Your lifetime allowance**
2. **Your annual allowance**

If you exceed these allowances, your benefits may be subject to a tax charge.

Even if you're not close to the current limits now, you may need to consider your overall position.

In this guide we focus on the annual allowance and our Lifetime Allowance Quick Guide covers the lifetime allowance in more detail.

Annual Allowance (AA) and Lifetime Allowance (LTA) are complex and our guides can only give you an overview. The key thing to remember is that you are urged to seek financial advice as soon as possible if you think you may be affected by AA or LTA.

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What do we mean?

Below are some high level explanations of some of the terms we use in this leaflet.

Adjusted income – your gross taxable income plus your pension contributions and relevant adjustments.

Annual allowance – the value of pension savings you can make each year without incurring a tax liability.

Lifetime allowance – the amount of pension saving you can build during your working life without incurring a tax charge.

Lifetime Allowance Protection – you have applied and been granted a tax free lifetime allowance higher than the standard lifetime allowance.

Pension input growth – this includes:

- any increase in the notional value of your scheme benefits;
- any added years AVCs you pay; and
- any other pension savings you make, including your state pension.

Threshold income – your pensionable pay less your pension contributions and relevant adjustments.

Unprotected member – someone who has joined the 2015 scheme and is no longer earning benefits in the pre-2015 arrangement.

What are the changes and how might they affect you?

There are two key changes that came into effect from 6 April 2016:

1. The lifetime allowance reduced from £1.25 million to £1 million. We expect the lifetime allowance to stay at this level until 2018 and then begin to rise in line with increases to the Consumer Prices Index (CPI). We explain what this might mean for you in our ‘Lifetime Allowance Quick Guide’
2. For the first time, the annual allowance will depend on your income and will reduce from £40,000 a year if your ‘adjusted income’ is more than £150,000 a year. Your annual allowance will not reduce if you have a threshold income of £110,000 or less (it will remain at £40,000).

Pension input growth

You will need to assess and consider giving your financial adviser or accountant a Pension Savings Statement we will provide a statement on request but will send one to you automatically if:

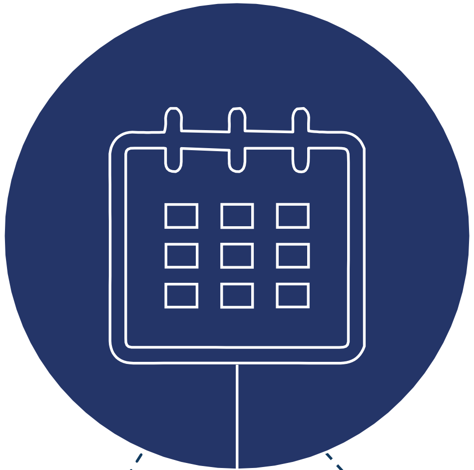
- you breach the £40,000 annual allowance.

Remember, this will only cover your membership in a Scottish public service pension scheme (including any benefits you have transferred in from another arrangement).

You need to ask for the same information from the administrators of any other scheme you have benefits in, including any cross border schemes that you have not transferred across. Your state pension is not included.

Annual allowance

Until now this allowance has been the same for all scheme members but from 6 April 2016, this allowance may reduce for high earners.



How does this work in practice?

If your threshold income is over £110,000 and your adjusted income is over £150,000 your annual allowance will reduce by £1 for every £2 of adjusted income over £150,000.

The maximum reduction is £30,000, which would leave you with a reduced annual allowance of £10,000 a year. We’ve summarised the impact of this in the table below.

Threshold income	Adjusted income	Annual allowance
Below £110,000	**N/A**	**£40,000**
Above £110,000	**Below £150,000**	**£40,000**
Above £110,000	**Between £150,000 and £210,000**	**Reduces by £1 for every £2 by which your threshold income exceeds £150,000**
Above £110,000	**Above £210,000**	**£10,000**

Your annual allowance is measured across a period of time, known as the Pension Input Period (PiP). From 6 April 2016 the PiP for all UK pension schemes will run in line with tax years.

"You should contact your financial adviser as soon as possible If you think you may be affected by the Annual Allowance."

Am I affected by the annual allowance and if so, what is the cost?

Whether or not you are affected can depend on number of things, including your level of pay, the size of any pay rises, increases in the cost of living and how much service you have. There are two key points to remember:

1. **You must take into account all your income, including income which is not pensionable.**
2. **If you're an unprotected member and you receive a pay rise, you may see a significant PiP in both the pre and post 2015 schemes. This places you in a higher risk of breaching the annual allowance.**

Everyone's circumstances will be different of course, if your threshold earnings are £110,000 or more you are already likely to be close to seeing your annual allowance begin to taper.

If your threshold earnings are a little less than £160,000, with 30 years' scheme membership and you are awarded a 1% pay rise you are likely to be see your annual allowance fall to £10,000. *

The table below provides some other broad examples of how various income levels might affect the annual allowance

Threshold income	Adjusted income	Reduced annual allowance
£100,000	N/A	N/A
£110,000	£147,000	N/A
£113,000	£150,600	£39,700
£150,000	£200,000	£15,000
£170,000	£227,000	£10,000

* based on membership of 30 years, with CPI and salary inflation both at 2%

What should you do now to protect your retirement savings?

If you think you may be affected by the Annual Allowance, it's important that you speak to your financial adviser as soon as possible.

HMRC has put arrangements in place to help you which are too complex to fully cover here although we have summarised some of them for you.

Your 10 second summary

The allowances for making tax-efficient pension savings has reduced.

We expect more members to be restricted by these allowances than may have been in the past.

You are urged to speak to your financial adviser or accountant as soon as possible if you think you are affected by the Annual Allowance.

Do you have benefits in a private sector pension scheme?

If you have previously worked in the private sector and been a member of a Defined Contribution (DC) scheme, you can now take these benefits in cash if you wish but there may be an even greater impact on your annual allowance arrangements if you do.

If you do have DC benefits and intend to use them to draw down cash, then you should seek further advice before making a decision. Your annual allowance could be reduced by £10,000 drawing down on your pension savings.

The information in this guide is based on our understanding of the tax and legal position and does not allow for any changes that may be announced after the date of publication. For more information on how your own particular circumstances may be affected, please contact us. This document is for reference purposes only and does not constitute financial advice. It is your responsibility to ensure that you pay any tax due on your pension savings.

You are also responsible for paying this tax unless you qualify to elect for scheme pays.

We recommend that you take independent financial advice from a registered adviser, who can assess and quantify the extent of any tax liability that is due. You can find a list of independent financial advisers at www.unbiased.co.uk