

ADVISER GUIDE

Lifetime allowance protection guide

In this guide:

Lifetime allowance basics	2
Protections overview	2
Primary protection	3
Enhanced protection	3
Fixed protections	4
Individual protections	5
Protection combinations	5
Late applications	6
Enhancement factors	6
Using the protections	7
Interactions when using protections	9

The information contained in this guide is based on our understanding of current law, practice and taxation which may be subject to change. Tax treatment depends on individual circumstances and rules may change.

Lifetime allowance basics

There is no absolute limit placed on the level of benefits that an individual can build up in UK registered pension schemes, but there was a maximum limit on the level of benefits that a person can draw without triggering certain tax charges. This limit was known as the lifetime allowance, and taking benefits above this level will incur a Lifetime Allowance Tax charge.

Pension savings were tested against the lifetime allowance at certain points in time; these relate primarily to accessing pension benefits, but can also apply at age 75, on death and in limited circumstances to increases in scheme pensions.

The table below shows the level of the lifetime allowance from when it was first introduced in 2006/07. In the March 2021 Budget it was announced that the lifetime allowance would be frozen at its current level of £1,073,100 for tax years 2021/22 to 2025/26.

2006/07	£1,500,000	2014/15	£1,250,000
2007/08	£1,600,000	2015/16	£1,250,000
2008/09	£1,650,000	2016/17	£1,000,000
2009/10	£1,750,000	2017/18	£1,000,000
2010/11	£1,800,000	2018/19	£1,030,000
2011/12	£1,800,000	2019/20	£1,055,000
2012/13	£1,500,000	2020/21	£1,073,100
2013/14	£1,500,000	2021/22	£1,073,100

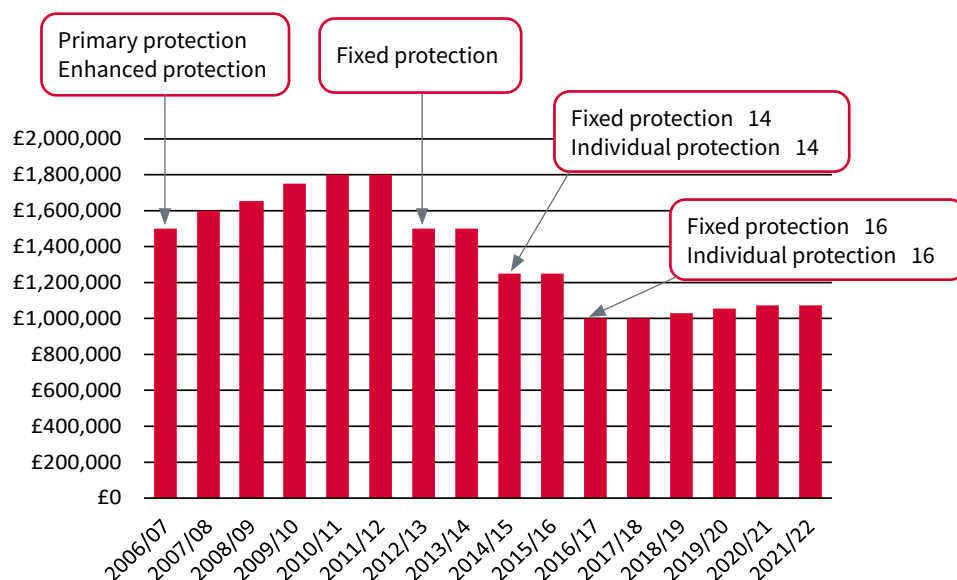
The lifetime allowance no longer exists. It has been replaced by the lump sum allowance and the lump sum and death benefit allowance.

Protections overview

When the lifetime allowance was introduced as part of pension simplification in 2006, two forms of protection were put into place so those who had already saved larger amounts into pensions before the allowance was introduced would not be penalised when they came to take benefits. These are primary protection and enhanced protection.

On three occasions since 6 April 2006, we have had further cuts to the lifetime allowance, and on each occasion new protections have been made available to protect those who had saved based on the expectation of a higher lifetime allowance. These are the fixed protections and the individual protections.

Lifetime allowance protections



Primary protection

Primary protection was available for those who had total pension savings of more than £1,500,000 at 5 April 2006. This form of protection gives individuals an enhancement factor that increases their personal lifetime allowance. This factor was calculated with reference to the individual's pension rights on 5 April 2006 and the lifetime allowance of £1,500,000 as introduced. The factor was therefore calculated as follows:

$(\text{pension rights at 5 April 2006} - £1,500,000) / £1,500,000$

The factor was always rounded up to two decimal places, so a figure of 0.231 would become 0.24.

Example

Pension rights @ 5 April 2006 = £1.75m
 $(£1.75\text{m} - £1.5\text{m}) / £1.5\text{m} = 0.166$
Additional lifetime allowance factor = 0.17

When primary protection was granted, HMRC issued a certificate to the member showing an enhancement factor. The reference number from this certificate needs to be given to the pension scheme administrator at benefit crystallisation events for the member to use their protection.

When primary protection was introduced, those who held this type of protection were entitled to a pension commencement lump sum (PCLS) of 25% of the standard lifetime allowance – not their personal lifetime allowance. From 2012/13 onwards, the PCLS is limited to a maximum of 25% of the higher of £1,500,000 or the standard lifetime allowance.

It is also possible to hold primary protection with lump sum protection. This was only possible if the individual's lump sum pension rights were more than £375,000 at 5 April 2006. If lump sum rights are also protected, this will be stated on the protection certificate from HMRC as a monetary figure.

Except in some pension sharing cases, primary protection cannot be lost once it has been granted, and it is not affected by the transfer of funds between registered pension schemes. Members with primary protection can continue to make contributions. The deadline for applying for primary protection was 5 April 2009 – but see the section on late applications below.

Enhanced protection

Enhanced protection was available to anyone regardless of the level of pension savings at 5 April 2006. However, the protection is lost if there is any relevant benefit accrual or any contributions are made on or after 6 April 2006. Where this protection is held, no lifetime allowance charges can arise regardless of the size of funds being crystallised.

When enhanced protection was granted, HMRC issued a confirmation certificate with a reference which must be given to the pension scheme administrator when the member uses their protection.

When enhanced protection was introduced, the PCLS was limited to 25% of the standard lifetime allowance, not the full protected fund value. Like with primary protection, from 2012/13 onwards the PCLS is limited to a maximum of 25% of the higher of £1.5 million or the standard lifetime allowance

Again, like primary protection it is also possible to hold enhanced protection with lump sum protection if the individual's lump sum pension rights were more than £375,000 at 5 April 2006. However, with enhanced protection the lump sum rights will be expressed as a percentage. When this percentage is stated on the protection certificate, the member is entitled to that percentage of their fund as a PCLS regardless of the size of fund they are crystallising. The percentage can be more or less than 25%.

Example

Pension rights @ 5 April 2006 = £2m
Lump sum rights @ 5 April 2006 = £400,000
Protected lump sum rights = 20%

If enhanced protection is lost for any reason, the exemption from the lifetime charge at any previous benefit crystallisation events is not affected; they are not reassessed retrospectively. Generally, transfers between UK registered pension schemes will not cause a loss of enhanced protection.

If protection is lost, HMRC must be notified within 90 days, or fines may be issued. The deadline for applying for enhanced protection was 5 April 2009.

Fixed protections

There are three forms of fixed protection, each introduced when there was a cut to the standard lifetime allowance. The first was just known as ‘fixed protection’, although it is commonly referred to as ‘fixed protection 2012’ or ‘FP12’ now to distinguish it from the later versions. 2014 (‘FP14’) and 2016 (‘FP16’) versions followed.

All the fixed protections operate in the same way, but they give different levels of protection. There was no requirement for a minimum fund size at any particular date, but the protection is lost if there is any relevant benefit accrual or any contributions are made after the application deadline (or 6 April 2016 for FP16).

	Level of protection	Application deadline
Fixed protection 2012	£1.8 million	5 April 2012
Fixed protection 2014	£1.5 million	5 April 2014
Fixed protection 2016	£1.25 million	5 April 2025

There is no separate PCLS protection available with any of the fixed protections. The maximum PCLS available will always be 25% of the applicable protected amount.

HMRC issued certificates to those who have been granted FP12 or FP14. Applications for FP16 are still open. This is an online process and a reference number is issued rather than a certificate. The individual will need to provide this reference to their scheme administrator when they wish to rely on the protection, and there is a look-up service for the administrator to check the protection held.

If any of the fixed protections are lost, the individual must notify HMRC. For FP12, this must be within 90 days of the loss of protection; for FP14 or FP16, this is within 90 days of when they could first reasonably be expected to have known they had lost their protection. HMRC may issue fines if these deadlines are not adhered to.

Individual protections

When the lifetime allowance was cut in 2014, a new form of protection was introduced – individual protection 2014 ('IP14'). Two years later, at the next reduction, individual protection 2016 ('IP16') was introduced. Both versions work in the same way, but different limits apply.

To qualify for the protection, pension savings needed to be in excess of the new standard lifetime allowance being introduced. The level of protection given would be the individual's total pension rights immediately before the cut in the standard lifetime allowance (the relevant date), up to a maximum of the outgoing standard lifetime allowance.

	Minimum fund value	Relevant date	Maximum level of protection	Application deadline
Individual protection 2014	£1.25 million	5 April 2014	£1.5 million	5 April 2017
Individual protection 2016	£1 million	5 April 2016	£1.25 million	5 April 2025

Like primary protection, both the individual protections allow contributions to still be made, and can only be lost under a pension-sharing order on divorce.

There is no separate PCLS protection available for either of the individual protections. The maximum PCLS available will always be 25% of the individual's protected amount.

Where IP14 is held, HMRC will have issued a certificate detailing the protected amount. For IP16, the application process is online and a reference is issued. The pension scheme administrator can use this to look up the member's individual level of protection. Applications for IP14 closed on 5 April 2017 but it is still possible to apply for IP16 and no deadline has been set.

Protection combinations

It is also possible to hold more than one type of protection at a time. The table below shows the combinations of protections that can be held.

	PP	EP	FP	FP14	IP14	FP16	IP16
PP	-	✓	X	X	X	X	X
EP	✓	-	X	X	✓	X	✓
FP	X	X	-	X	✓	X	✓
FP14	X	X	X	-	✓	X	✓
IP14	X	✓	✓	✓	-	✓	X
FP16	X	X	X	X	✓	-	✓
IP16	X	✓	✓	✓	X	✓	-

When primary and enhanced protection are held together, the certificate will state "Enhanced Protection with dormant Primary". Enhanced will always take precedence, but if it is revoked or lost for any reason, then the primary protection will come into force.

Similarly, if either of the individual protections are held alongside enhanced protection or any of the fixed protections, then it will be dormant until the enhanced/fixed protection is revoked or lost. Certificates do not state that individual protection is held in this situation, but a new certificate or reference number is issued as evidence once the other form of protection is revoked or lost.

Late applications

Regulations allow for late applications for primary and enhanced protection where:

- there is a reasonable excuse for not giving the notification by the closing date; and
- the notification is completed without unreasonable delay once the reasonable excuse has ceased.

If HMRC refuses to consider the late application, an appeal process through the tax tribunals is available.

There is no such provision for late applications relating to any of the fixed or individual protections.

Enhancement factors

There are certain circumstances when individuals may be entitled to one or more lifetime allowance enhancement factors (LAEFs). Generally, these relate to pension rights held that have already been tested against the lifetime allowance, or to benefits that have not had the advantage of receiving tax relief in the UK.

Pension credit enhancement factor

Where an individual receives a pension credit following a pension sharing order on divorce, and that credit relates to crystallised pension rights that came into payment on or after 6 April 2006, the recipient will be entitled to a pension credit enhancement factor. This is because these pension rights will have already been tested against the lifetime allowance in the hands of their ex-spouse.

Recognised overseas scheme transfer factor

Where a transfer is made from a recognised overseas pension scheme into a UK registered pension scheme, an enhancement factor can be claimed as the rights will not generally have benefitted from tax relief in the UK.

If any funds in the overseas scheme have received UK tax relief at any point, these are deducted from the transfer amount for the purposes of calculating the enhancement factor

Non-residence factor

If an individual accrues rights in a UK registered pension scheme during a period when they are a relevant overseas individual, and therefore do not receive tax relief in relation to these rights, then they will qualify for the non-residence factor in relation to rights built up in the relevant tax years.

To calculate the LAEF, the relevant amount is divided by the lifetime allowance at the time the rights were acquired. For pension credit enhancement factors, this will be the tax year the pension-sharing order was implemented and funds transferred into the member's name. For the recognised overseas scheme transfer factor, it will be the year the transfer comes into the UK scheme, and for the non-residence factor it will be the earliest of:

- immediately before their first benefit crystallisation event;
- the date they ceased to be a relevant overseas individual; or
- the date when benefits ceased to accrue.

As with primary protection, the figure is always rounded up to two decimal places, so a figure of 0.3727 becomes 0.38.

The below are examples of historical enhancement factors that could apply to pensions.

Example

Pension credit of £400,000 in 2022/23
 $\text{£}400,000 / \text{£}1,073,100 = 0.3727$
Rounded up = 0.38

If any of the fixed or individual protections were held, then the individual's personal lifetime allowance would be used to calculate the enhancement factor, instead of the standard lifetime allowance.

Example

If FP14 held
Pension credit of £400,000 in 2022/23
 $\text{£}400,000/\text{£}1,500,000 = 0.2667$
Rounded up = 0.27

When someone qualifies for an enhancement factor, they have five years following 31 January in the tax year following the relevant tax year to apply. So if someone had a QROPS transfer-in in 2022/23 tax year, they would have until 31 January 2029 to apply.

Using the protections

When using any of the protections, the member will need to provide evidence of that protection to the scheme administrator. For all the protections that were introduced up to and including 2014, HMRC issued certificates. For the 2016 protections, the process is all online and reference numbers were issued on successful application. The relevant certificate or reference number will need to be provided to the scheme administrator for the member to make use of their protection.

Using primary protection

Since 2012/13, when the lifetime allowance was cut from £1.8 million to £1.5 million, the primary protection factor has always been applied to the 'underpinned' lifetime allowance of £1.8 million, rather than the standard lifetime allowance. This will continue to be the case until the standard lifetime allowance increases above £1.8 million. This was designed to stop those who held primary protection from being worse off when the standard lifetime allowance was cut.

Where no lump sum protection is held, someone with primary protection could originally only take a maximum PCLS of 25% of the standard lifetime allowance, not their personal enhanced lifetime allowance. This meant the first lifetime allowance cut did reduce the amount of PCLS available. From 2014/15 onwards, those with primary protection can have PCLS of up to 25% of £1.5 million (£375,000). This will continue to be the case until the standard lifetime allowance rises above this level.

Example

Pension rights @ 5 April 2006 = £1.75m
 $(\text{£}1.75\text{m} - \text{£}1.5\text{m})/\text{£}1.5\text{m} = 0.166$
Additional lifetime allowance factor = 0.17

Fully crystallises in 2021/22
Fund value £2m
Protected LTA = $\text{£}1.8\text{m} + (0.17 \times \text{£}1.8\text{m}) = \text{£}2,106,000$
Max PCLS = $25\% \times \text{£}1.5\text{m} = \text{£}375,000$
Drawdown fund = $\text{£}2\text{m} - \text{£}375,000 = \text{£}1,625,000$

In the example above, there is no lifetime allowance charge as the value of the protection (£2,106,000) is greater than the value of the funds being crystallised (£2 million).

To further complicate matters, regulations state that scheme administrators must report lifetime allowance usage on the standard lifetime allowance, not the protected amount.

Example

Fully crystallises in 2021/22
Fund value £2m

Lifetime allowance usage reported as:

PCLS: $\text{£}375,000/\text{£}1,073,100 \times 100 = 34.94\%$

Drawdown: $\text{£}1,625,000/\text{£}1,073,100 \times 100 = 151.43\%$

Total lifetime allowance usage = 186.37%

This can lead to confusion, as in the example above the individual will receive a letter stating they have used 186.37% of the lifetime allowance, when in fact they still have £106,000 of lifetime allowance still available (albeit they can take no further PCLS).

Where lump sum protection is held alongside primary protection, it is expressed as a monetary amount. This monetary amount is revalued when a PCLS is paid. Currently the revaluation is based on the underpinned lifetime allowance of £1.8 million – i.e. £1.8 million/£1.5 million where £1.5 million is the lifetime allowance when the protection was obtained. If the lifetime allowance rises above £1.8 million, the revaluation will be based on the standard lifetime allowance/£1.5 million.

In practice, this means that the monetary amount stated on the primary protection certificate is uplifted by 20% as $\text{£}1.8 \text{ million}/\text{£}1.5 \text{ million} \times 100 = 120\%$.

Example

Protected PCLS = £500,000

Max PCLS = $\text{£}500,000 \times \text{£}1.8\text{m}/\text{£}1.5\text{m} = \text{£}600,000$

Using enhanced protection

Enhanced protection gives unlimited protection, so there are no calculations involved in working out the maximum protection available. Like primary protection, the lifetime allowance usage is based on the standard lifetime allowance.

Where no PCLS protection is held, the maximum PCLS available will be 25% of £1.5 million (£375,000), until such a time as the standard lifetime allowance is higher.

If PCLS protection is held, this is stated as a percentage of the amount being crystallised and there is no upper limit.

Using fixed protections

Using any of the fixed protections is relatively straightforward. The member's lifetime allowance will be the relevant amount depending on which of the protections is held – £1.8 million for FP12, £1.5 million for FP14 or £1.25 million for FP16.

The maximum PCLS will always be 25% of the funds crystallising up to the protected amount, and the lifetime allowance usage is reported based on the protected amount.

Using individual protections

Using either of the individual protections is very similar to using the fixed protections; the only difference is that there will be a personalised level of protection. The maximum PCLS will still be 25% of the funds crystallising up to the protected amount, and the lifetime allowance usage is reported based on the individual protected amount.

Using enhancement factors

Where an enhancement factor is held, that factor will be applied to the standard lifetime allowance when benefits are crystallised. PCLS will still be based on a maximum of 25% of the funds crystallising up to the standard lifetime allowance.

Interactions when using protections

Enhanced with dormant primary protection

It was common for individuals with pension savings in excess of £1.5 million on 5 April 2006 to apply for both enhanced and primary protection. Where this is the case, their protection certificate will state they have “Enhanced Protection with dormant Primary”. In most cases, using enhanced protection will be the better option, but if the fund value is below the level of primary protection, there are circumstances where more PCLS may be available under the primary protection.

Example

5 April 2006 fund value £2m; £600,000 PCLS

Enhanced protection with 30% PCLS

Dormant primary protection with £600,000 PCLS

Primary protection factor = $(£2m - £1.5m)/£1.5m = 0.34$

Personal lifetime allowance under primary = $£1.8m + (0.34 \times £1.8m) = £2,412,000$

	£2,200,000	£2,300,000	£2,400,000	£2,500,000
Enhanced PCLS	£660,000	£690,000	£720,000	£750,000
Primary PCLS	£720,000	£720,000	£720,000	£720,000

As we can see in the example above, where the fund value is below £2.4 million, primary protection offers a higher level of PCLS. Under primary protection, contributions are allowed, so it would also be possible to top up to the protected amount immediately before taking benefits, without incurring any tax charges. This would not, however, increase the PCLS available. It is possible to revoke enhanced protection without making contributions by notifying HMRC.

Fixed with dormant individual protection

Similar to enhanced and primary, it is possible to hold any of the fixed protections with either of the individual protections dormant to it. This would not be stated on the certificate, but if the fixed protection is revoked, HMRC issue a new certificate or reference number confirming that individual protection is held.

The level of fixed protection will usually be higher than the individual protection, but unlike individual protection no contributions are permitted. Individual protection is generally used when the fund value has dropped, as it allows contributions to be made to top up pension savings to the level of the individual protection before crystallising.

Example

Fixed protection 2014 held - £1.5m

Dormant individual protection held - £1.4m

Fund value when crystallising is £1.35m

Individual protection allows a contribution of £50,000 to be made with no lifetime allowance charge when accessed.

PCLS will increase from $25\% \times £1.35m = £337,500$ to $25\% \text{ of } £1.4m = £350,000$

Enhancement factors

It is possible for someone to have multiple enhancement factors, and/or to hold other forms of protection in conjunction with a lifetime allowance factor.

If multiple lifetime allowance factors are held, or one or more are held in addition to primary protection, then the factors are simply added together and applied to the relevant lifetime allowance (in most circumstances this will be the lifetime allowance when benefits are crystallised). When primary protection is held, the factor is applied to the underpinned lifetime allowance of £1.8 million.

Where any of the fixed or individual protections are held, the lifetime allowance factor is applied to the personal lifetime allowance. It is not possible to have a lifetime allowance factor with enhanced protection, as benefits are already fully covered and no lifetime allowance charge can arise.

Example

LTAEF = 0.25; FP16 held

Personal LTA = £1,250,000 + (0.25 x £1,250,000) = £1,562,500