Fact Sheet

tpo the private office

The Money Purchase Annual Allowance

The introduction of pension freedoms on 6 April 2015 opened the door to greater flexibility and freedom in how individuals consolidate, contribute, invest and draw down from their pension funds.

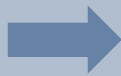
New pension regulations mean greater flexibility and freedom in how you consolidate, contribute, invest and draw down from pension plans.

More choice with contributions

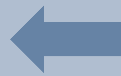
More choice with investments

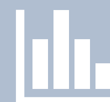
More choice with how you take income

Annuity



Up to 25% tax free
Take part of your pension as a lump sum**





Drawdown

Flexible Income Choices

Choose whether to take an annuity with a guaranteed income for life, take a set income each year with a capped drawdown*, or the flexi-access option which sets no limits on the income taken.

Capped drawdown

Flexi-access drawdown

*Available only to those with capped drawdown prior to April 2015 where contract allows additional funds to be added. The value of investments can go down as well as up and is not guaranteed.
**Subject to an overall limit of £268,275 in most cases.

Many individuals have chosen to take advantage of these new freedoms and access some of their accumulated pension wealth whilst continuing to work and fund additional pension contributions. With an ever increasing pension tax relief bill to meet HM Revenue and Customs were concerned that some of this pension wealth may be used to fund these additional pension contributions enabling a **second bite of income tax relief.** This led to the introduction of the **Money Purchase Annual Allowance** which restricts the payment of new tax efficient contributions to a money purchase arrangement to **£10,000 per annum** for affected individuals.

Who does this affect?

The Money Purchase Annual Allowance only affects individuals who have accessed their money purchase funds using one of the flexible options since 6 April 2015. Capital can still have been extracted from a money purchase pension plan without triggering the Money Purchase Annual Allowance in the following ways:

- Purchase of a conventional pension lifetime annuity which cannot be varied after purchase.
- Withdrawing all capital from a pension using the 'small pots' rules. This enables an individual to 'cash in' up to three individual pension plans during their lifetime (after the age of 55) provided the value of each plan does not exceed £10,000. The small pot facility can be used an unlimited number of times for occupational schemes subject to the same monetary restriction for each arrangement.
- For clients in capped drawdown prior to 6 April 2015 – remain in capped drawdown and maintain income withdrawals within the Government Actuary's Department (GAD) limits.
- Extract a Pension Commencement Lump Sum (tax free cash) only from your pension.
- Disqualifying pension credits are funds which are created by a pension sharing order on divorce, when linked to a crystallised fund, i.e. where the recipient is disqualified from taking any Pension Commencement Lump Sum (PCLS).
- Income paid via flexi-access drawdown from such a fund will not trigger the Money Purchase Annual Allowance.

Technical details

- Individuals who have triggered the Money Purchase Annual Allowance still have an **Alternative Annual Allowance** of up to £50,000 per annum, in addition, which can be applied to the funding of a defined benefit (final salary) scheme. Normal tapering rules apply for high earners.
- Carry forward of unused annual allowances cannot be applied to increase the level of contribution to a money purchase pension plan once the Money Purchase Annual Allowance has been triggered. Carry forward remains available for funding to defined benefit schemes.
- Once the Money Purchase Annual Allowance has been triggered it affects the tax year in which benefits have been accessed from the date that funds are flexibly accessed and all future tax years.

Tax charge for excess contributions

Excess contributions are added to other taxable income in the year of payment as the 'top slice' of income, meaning that an income tax charge of up to 45% could arise. This tax charge is borne by the individual regardless of how the excess contribution was funded (but may, in some cases, be able to be paid out of the pension plan benefits). So:

- 45% on any of the 'excess amount' that falls into the additional 45% income tax band,
- 40% on any of the 'excess amount' that falls into the higher 40% income tax band, and
- 20% on any of the 'excess amount' that falls into the basic 20% income tax band.

From 6 April 2017, different tax bands apply for Scottish residents compared to the rest of the UK; there are currently five income tax bands. When calculating the annual allowance tax charge for Scottish residents, the applicable income tax bands and rates of income tax should be used.

Paying the excess charge

The Annual Allowance tax charge is normally collected through the self-assessment process, but it's sometimes possible for this charge to be paid from pension benefits. Pension schemes can choose to offer this facility in any circumstances, but are only required to pay the charge on behalf of a member if:

- The full Annual Allowance (not just the Money Purchase Annual Allowance) under that specific scheme was exceeded i.e. funding in excess of £60,000 has been made in that year,
- Based on the excess over the Annual Allowance, the tax charge is more than £2,000, and
- The member elects for the charge in respect of the excess contribution above £60,000 to be met from their pension benefits under the scheme and makes a request within the prescribed timeframe.

IMPORTANT

As noted above, the scheme is only required to pay the excess charge in respect of the excess funding above £60,000.

It may agree to pay excess charges for tapered clients below this threshold under a voluntary arrangement but cannot be compelled to do so.

Notification Requirements – HM Revenue & Customs

If an individual accesses pension benefits flexibly and triggers the Money Purchase Annual Allowance, the pension scheme administrator has to provide them with a statement to this effect within 31 days of the event.

It is then **the individual's responsibility** to inform all other defined contribution and hybrid pension schemes where they are an active member (making contributions) that they are restricted by the Money Purchase Annual Allowance within 91 days. **Failure to make notification can lead to a £300 fine and daily penalties of up to £60 for every day of delay in providing notification.**

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Please also note that every care has been taken to ensure that the information provided in this article is correct and based on our understanding of current law and HM Revenue and Customs practice as at April 2023. It is not intended to provide individual advice and independent confirmation should be obtained before acting upon the information given.

FP: 0223021