Pensions taxation factsheet

This factsheet is for members of the Scottish Enterprise Pension and Life Assurance Scheme ('the Scheme') only. It explains:

- How the Annual Allowance works;
- How members can elect for the Scheme to pay some or all of their Annual Allowance charge (through the Scheme Pays facility) and the deadlines for applying;
- How a Scheme Pays election will affect your benefits; and
- What the Lump Sum Allowance and Lump Sum and Death Benefit Allowance is (which replaced the Lifetime Allowance).

Important

While this factsheet tells you about the options available to you from the Scheme, it does not provide you with any advice on which option to take or how best to exercise your options. The Trustee cannot provide you with financial advice.

If you need advice on tax matters, you can contact a tax or financial adviser before making a decision. You can find an IFA through the following website: **www.unbiased.co.uk.** You may be charged a fee for any advice.

This factsheet reflects our understanding of current legislation , HMRC's methodology and the trust deed and rules. This publication is for general guidance only.

1. What is the Annual Allowance?

The Annual Allowance is a threshold which limits the amount your pension can grow each year before tax charges apply.

2. How much is the Annual Allowance?

The standard Annual Allowance is currently £60,000. However, this is tapered for high earners.

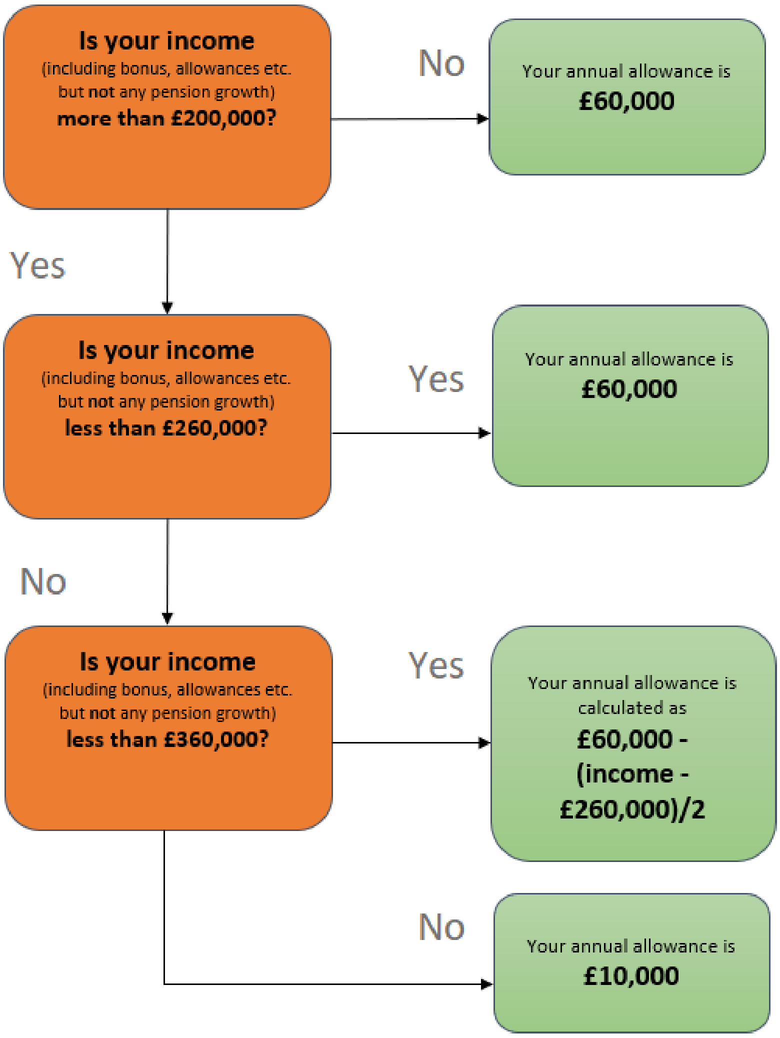
3. How does tapering impact the Annual Allowance?

From April 2016 the Annual Allowance may be smaller if you have income above a certain amount. This is known as the Tapered Annual Allowance.

The assessment of whether you are subject to the Tapered Annual Allowance can be complex. From 6 April 2023[1], for each £2 that your adjusted income (broadly your income plus your pension growth) exceeds £260,000[2] you will lose £1 from your Annual Allowance. If your adjusted income is more than £360,000[2] you will have a Tapered Annual Allowance of £10,000[2]. Your Annual Allowance cannot reduce to lower than £10,000[2] on account of this tapering. The flowchart below might help you understand this.

[1] Please note that the thresholds were different prior to 6 April 2023

[2] Income and annual allowance thresholds are based on the tax year (i.e. earnings and annual allowance limits are for the period of 6 April 20XX to 5 April 20XX+1)



4. How is my pension growth calculated?

Pension growth is calculated as the difference in the value of your Scheme benefits at the beginning of the tax year increased with the Consumer Prices Index (CPI) against the value of your Scheme benefits at the end of the tax year. The growth in your Scheme pension is multiplied by a factor of 16 and added to the growth in your lump sum.

(Pension at end of year – Pension at start of year increased by CPI) X Government valuation factor of 16 PLUS Lump sum at end of year) – Lump sum at start of year increased by CPI

5. How do I know whether my pension growth has exceeded the Annual Allowance

The Scheme will notify you automatically if your pension growth in the Scheme exceeds the standard Annual Allowance. If you are subject to a reduced Annual Allowance (because of the **Tapered Annual Allowance**) then you might need to request a pension growth statement to check your position. This is because schemes have no way of knowing exactly what your tapered allowance is. The pensions saving statement will only consider your benefits earned in the Scheme. If you have benefits elsewhere, these should also be taken into consideration when assessing whether you exceed the Annual Allowance.

The pension savings statement will notify you of your benefit growth in the current tax year together with the previous three tax years. This is so you can calculate whether you have any unused Annual Allowance from these years that can be carried forward and used to increase the Annual Allowance in the current tax year. This may offset, in part or in full, any total pension growth more than the Annual Allowance.

6. What about my contributions to other pension arrangements?

Your total pension savings are subject to the Annual Allowance test so any contributions you pay to other registered pension schemes will also need to be allowed for when calculating how much your pension savings have grown by in any one year.

Please note that whilst in a defined benefit scheme (such as the Scottish Enterprise Pension and Life Assurance Scheme) it is your pension growth that is tested against the Annual Allowance. In a defined contribution scheme (such as a personal pension plan) it is your gross pension contributions that are tested against the Annual Allowance.

7. What happens if I retire during the tax year?

If you retire during the tax year, then your benefits will be assessed against the Annual Allowance or Tapered Annual Allowance to calculate pension growth from the start of the tax year until your date of retirement.

8. What is carry forward?

If your pension growth exceeds the Annual Allowance or Tapered Annual Allowance in any one year you can "look back" up to three previous tax years to see if you have any unused allowance from these years.

If you are subject to the taper, you can only carry forward unused allowance from a tapered year up to the tapered amount (not up to the standard limit of £60,000). For example, if your Tapered Annual Allowance is £20,000 and you have pension growth of £11,000 you would be able to carry forward £9,000 only.

This means that even if your pension growth exceeds the Annual Allowance or Tapered Annual Allowance threshold in any one year, you may not have any extra tax to pay, depending upon how much you can carry forward.

9. What happens if my pension growth is greater than the Annual Allowance?

Normally, an individual will need to pay an Annual Allowance tax charge if their pension growth in a tax year exceeds the Annual Allowance limit that applies to them, and they don't have enough unused allowance to carry forward from the previous three tax years. An Annual Allowance tax charge will apply to any excess.

In certain circumstances, an individual can elect for their pension scheme to pay part or all of the charge on their behalf from their pension savings. This is known as 'Scheme Pays' (**see question 12**).

10. What rate of tax applies?

If an Annual Allowance tax charge is due, it's payable at the same marginal rate as your taxable income and is dependent on any other taxable income you had during the tax year in which the Annual Allowance charge occurs. Scottish taxpayers are subject to an Annual Allowance tax charge based on Scottish income tax rates and tax bands.

11. How do I pay the tax charge?

An Annual Allowance tax charge may be settled in one of two ways:

- You can pay it direct to HM Revenue & Customs ("HMRC"); or
- You can use the "Scheme Pays" option, if you qualify, so that the tax charge is met by the Scheme on your behalf with an appropriate reduction then made to your benefits.

Whichever option you choose, you usually need to inform HMRC of the action you are taking by 31 January following the end of the relevant tax year – e.g. 31 January 2027 for an Annual Allowance tax charge incurred in the 2025/26 tax year. Further details on paying the tax charge are set out in **question 17**.

12. When can I use Scheme Pays?

There are conditions that need to be met for an individual to have the right to use the Scheme Pays facility.

You have the right to use Scheme Pays on a '**mandatory** basis' if:

- the value of your pension growth is greater than the standard Annual Allowance of £60,000;
- your Annual Allowance tax charge for the tax year exceeds £2,000;
- your election to use "Scheme Pays" is received within the required statutory deadline (the deadlines and process are set out in more detail under **questions 17 and 18** below); and
- you have not already taken all your benefits from the Scheme.

If these conditions are met, you can ask the Scheme to pay the tax charge for you, and your pension benefits will be reduced as explained under **question 14** below.

Pension schemes can allow access to the Scheme Pays facility where one or more of these conditions haven't been met – known as the '**voluntary** basis' – but are not required to do so.

Those subject to the Tapered Annual Allowance only have the right to use the Scheme Pays facility to pay a charge of £2,000 or more in respect of any excess that exceeds the standard Annual Allowance of £60,000. However, you are still able to ask the Scheme to meet charges below the standard Annual Allowance on a voluntary basis if the other conditions are met.

13. How much can I ask the Scheme to pay?

You can pay part of the charge yourself, with the Scheme covering the rest or, you can ask the Scheme to pay the whole charge.

If you have exceeded the Annual Allowance because of benefits built up in two or more pension arrangements, we will only pay a tax charge for any excess allowance built up in this Scheme.

14. Recovering the Annual Allowance charge

We recover the cost of paying your Annual Allowance charge by reducing your benefits when they are paid to you.

We record the amount of Annual Allowance charge paid by Scheme Pays as a 'notional negative account' on your pension record. In basic terms this is like the pension scheme 'loaning' you money now to pay your tax bill which you have to pay back with interest at a future date, either when you either retire or transfer out.

Interest is added to the amount of Annual Allowance charge paid from the Scheme until your benefits from the Scheme come into payment. Currently the interest applied each year is based on the previous September's Consumer Price Index (CPI) figure plus 2% p.a. We can change the amount of interest charged over time following guidance received from the Scheme Actuary.

It may be that you want to use Scheme Pays to meet an Annual Allowance charge for more than one tax year – if so, the notional account will be added to each time a tax charge is paid to HMRC by the Scheme for you.

At your retirement the total balance you owe, including all relevant interest will be deducted from your Scheme benefits. You can choose whether to pay this off using your accrued retirement lump sum or accept a reduction in your pension. In this case the negative account will be converted into a reduction to your pension using factors provided by the Scheme Actuary. These factors change each month in line with movements in market conditions and are typically reviewed every three years as part of the Scheme's actuarial valuation. There will be a corresponding reduction in the pension payable after your death to your spouse, civil partner, or other financial dependant.

When your pension benefits are reduced because of Scheme Pays it is the capital value of the reduced benefits that are tested against the Lump Sum Allowance and the Lump Sum and Death Benefit Allowance at retirement (see **questions 20 to 25** for future information on these allowances).

EXAMPLE

Mr A is member of the Scheme. The Scheme paid an Annual Allowance tax charge for him in respect of 2020/21 under the Scheme Pays option of £4,500. A 'notional negative account' was established at that time and is increased by interest until he comes to draw his benefits. By the time he comes to draw his pension benefits, in five years' time, the value of the notional negative account (including interest) has increased to £5,250 (note the interest applied is an example only). This would be offset from his benefits as follows:

- Value of Mr A's 'notional negative account': £5,250
- Scheme entitlement prior to the Scheme Pays reduction: pension of £30,000 p.a. plus lump sum of £90,000.
- If Mr A wants to settle this by reducing the pension he will receive:
    - The factor for converting the notional account into a pension reduction is £1 p.a. of pension per £25 of account (this factor is for illustration only; factors are reviewed from time to time and vary based on several factors including age at retirement)
    - The pension reduction is: £210 pa (= £5,250 / 25)
    - Then Mr A's reduced Scheme pension is: £29,790 p.a. (= £30,000 - £210)
- If Mr A wants to settle this by reducing his retirement lump sum he will receive:
    - A reduced retirement lump sum of: £84,750 (= £90,000 - £5,250)

15. What if I die before retirement?

If you die before your benefits become payable, the notional negative account will be cancelled, and will have no effect on any benefits payable to your dependants.

16. What if I take a transfer value?

If you leave and transfer your pension rights to another registered pension scheme, the transfer value is reduced to recover the total balance owed.

17. What do I need to do if I have an Annual Allowance charge?

You **do not** need to tell HMRC if your pension growth is below the Annual Allowance or above the Annual Allowance, but you have enough unused Annual Allowance from the previous three tax years to carry forward.

If you have an Annual Allowance charge you are responsible for providing information to HMRC using a self-assessment tax return. If you don't normally complete a self-assessment tax return, you'll need to register with

HMRC to complete one. HMRC has a help sheet which you may find useful, which you can find by searching for "HS345" on **www.hmrc.gov.uk.**

You will need to complete a self-assessment tax return by no later than 31 January following the tax year in question and confirm to HMRC the amount of any Annual Allowance charge which is to be paid by the Scheme.

You do not need to tell us if you pay your Annual Allowance tax charge directly to HMRC. Make sure you pay your Annual Allowance charge to HMRC by the deadline. You will be charged interest and may have to pay a penalty if your payment is late.

If you decide that you want us to pay your Annual Allowance charge in respect of the growth in your Scheme benefits, then you will need to complete a Scheme Pays Notification. You normally have until the following 31 July – or retirement if earlier – to notify the Scheme of the Annual Allowance tax charge to be paid on your behalf. Ensure that you fully understand the implications of making a Scheme Pays election on your future benefits before completing this.

This notification needs to include specific information required by the legislation and so, to ensure this is all provided, we have prepared a standard form for you to use. You will need to print this, complete it, and send it to the **Scheme Administrator, Hymans Robertson**, so that it is received within the timescales set out above.

This form, together with these guidance notes, is available on the Scheme's website **www.sepensions.co.uk**

We will acknowledge your form and confirm that arrangements have been made to pay the Annual Allowance tax charge due on your behalf. If you do not receive an acknowledgement within 1 month then please contact the **Scheme Administrator**.

18. What is the deadline for making a Scheme Pays election?

If you would like us to pay some or all of your Annual Allowance charge via the mandatory basis as describe in **question 12**, then we must receive your completed Scheme Pays notification on or before **31 July** following the January in which the Annual Allowance charge must be declared on your tax return. If you expect to retire before 31 July, the notification must be completed and sent to us before your benefits crystallise. Please find the "Scheme Pays Notification (Mandatory basis - Standard Annual Allowance limit and tax charge over £2,000)" on the Scheme's website **www.sepensions.co.uk.**

If you are applying to use Scheme Pays on a voluntary basis (for example, if you want the Scheme to meet the charge arising from the Tapered Annual Allowance) then legislation requires that you notify us before **31 January** in line with the timing for your self-assessment tax return. Please find the form "Scheme Pays Notification (Voluntary basis - Tapered Annual Allowance limit or tax charge less than £2,000)" on the Scheme's website **www.sepensions.co.uk**.

We **must** receive your notification by the above dates. It is not enough just to send your notification by the deadline.

19. Can I change the amount of a Scheme Pays election?

Once made, a Scheme Pays notification cannot be withdrawn. However, if the amount of the tax charge changes, you can change the election with a corrected amount. To change your original election, we have to receive a revised election form no later than the 31 July following the end of a period of four years from the end of the tax year to which the Annual Allowance charge relates. For example, this could occur if you estimated the amount of your Annual Allowance charge to meet the Scheme Pays deadline.

20. What is the Lump Sum Allowance?

The Lump Sum Allowance (“LSA”) is the maximum tax-free lump sum retirement benefits an individual can receive in their lifetime. It was introduced from 6 April 2024 and is currently set at £268,275. You can usually take up to 25% of the value of your pensions as a tax-free lump sum unless it’s more than the LSA.

21. What is the Lump Sum and Death Benefit Allowance?

The Lump Sum and Death Benefit Allowance (“LSDBA”) is the maximum tax-free lump sum retirement benefits that an individual and their beneficiaries (the person or people who get benefits after they die) can be paid in respect of an individual. It was introduced from 6 April 2024 and is currently set at £1,073,100.

22. How do the allowances work?

Any benefits you take as a tax-free retirement lump sum (sometimes referred to as a Pension Commencement Lump Sum or “PCLS”) will use some of both your LSA or LSDBA. The amount of each allowance used will be equal to the amount of tax- free lump sum you receive.

Any benefits you claim in the form of monthly pension payments or regular income will not use any of your LSA or LSDBA.

For example, if you were retiring and receiving a pension of £10,000 per year and a tax-free lump sum of £30,000 then you would use £30,000 of your LSA and £30,000 of your LSDBA. Any lump sum paid more than either of the new allowances will be subject to income tax through the PAYE system at an individuals’ marginal rate.

23. What happened to the Lifetime Allowance?

Before 6 April 2024, the Lifetime Allowance was the maximum amount of pension savings an individual could build up in their pension schemes without incurring an additional tax charge. The regime also set a maximum amount that could be taken as a tax-free lump sum whenever an individual claimed retirement benefits from a pension scheme. From 6 April 2024 the Lifetime Allowance was abolished and was replaced with two new allowances – the LSA and the LSDBA (further information on these allowances is provided **above**).

24. What if I had a protected Lifetime Allowance?

Some people may be able to protect their pension savings for a tax charge if they have a protected Lifetime Allowance (if you do, you should have a Lifetime Allowance Protection Certificate). Anyone with this protection will also have these new allowances enhanced to reflect this.

25. How will any benefits I claimed before 6 April 2024 affect my allowances?

If you claimed retirement benefits from a pension scheme prior to 6 April 2024 then that scheme will have told you the percentage of the Lifetime Allowance used by your benefits. That percentage of the Lifetime Allowance needs to be converted to an amount of the new allowances used. For most people who did not have a protected Lifetime Allowance that conversion is simply: % of Lifetime Allowance used x £1,073,100 x 25%.

Further information

More detailed information can be found on HMRC's website at **www.hmrc.gov.uk**

HMRC have published a Pensions Tax Manual and this can be found at:
www.hmrc.gov.uk/manuals/ptmanual/Index.htm

If you have any queries please do not hesitate to contact the Scheme administrator:

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