Environment Agency
Pension Fund

October 2023

The tax controls on pension savings

About this guide

The Environment Agency Pension Fund (EAPF) is part of the Local Government Pension Scheme (LGPS) and is governed by the LGPS regulations.

This guide is for all employees who have joined the LGPS and who want to know more about the tax issues that affect their pensions savings.

The LGPS is registered with HM Revenue and Customs (HMRC), which means that you receive tax relief on your contributions as they're deducted from your pay.

However, there are two HMRC limits on the amount of pension savings you can have before you may have to pay a tax charge. This is over and above any tax due under the PAYE system on your pension once it's in payment.

The two limits on pension savings are known as the annual allowance and the lifetime allowance; in this factsheet we'll take a brief look at these allowances. Most people will be able to save as much as they wish with full tax relief, as their pension savings will be less than these allowances.

What we'll cover in this factsheet

To make it easier to navigate through our factsheet, you can click on a topic below and you'll be taken straight to that section.

Annual allowance

What is the annual allowance?

The annual allowance (AA) is the amount your pension savings can increase in any one year before you may have to pay a tax charge.

Since April 2014, the AA was set at a level of £40,000. However, from 6 April 2023, the AA has increased to £60,000. The AA also applies in the year you take your benefits, although there's an exemption in the case of severe ill health retirement or on death.

The period over which pension savings are measured is the same as the tax year and runs from 6 April to 5 April. Generally speaking, any pension benefits you have in tax registered pension arrangements where you've paid contributions during the tax year (or your employer has paid contributions on your behalf) are included in calculating your pension savings in that tax year.

Even if the value of your pension savings increase by more than the AA in a year, you may not have to pay an AA tax charge. This is because you can use any unused AA from the last 3 years (known as Carry Forward) to offset any excess savings in the current year. To carry forward unused AA from an earlier year, you must've been a member of a tax registered pension scheme in that year.

Example showing how 'Carry Forward' works

Pension savings in the EAPF @ 5 April 2023 (2022/23)	£60,000

Tax year of pension savings	Pension savings in the EAPF for that tax year	Unused allowance from that tax year (Carry Forward)*
2021/22	£25,000	£15,000
2020/21	£28,000	£12,000
2019/20	£32,000	£8,000

'Gross' excess pension savings = £60,000 - £40,000 (2022/ annual allowance)
= **£20,000**

Total Carry Forward available = £15,000 + £12,000 + £8,000
= £35,000

In this example there will be no AA tax charge to pay as the Carry Forward is higher than the excess pension savings.

Where Carry Forward is used to offset excess pension savings, the earliest year is used first. Therefore, as only £20,000 of the member's Carry Forward was needed to completely offset their excess pension savings for 2022/23, this means that £15,000 of Carry Forward from 2021/22 still remains, which could be used to offset any excess pension savings in 2023/24.

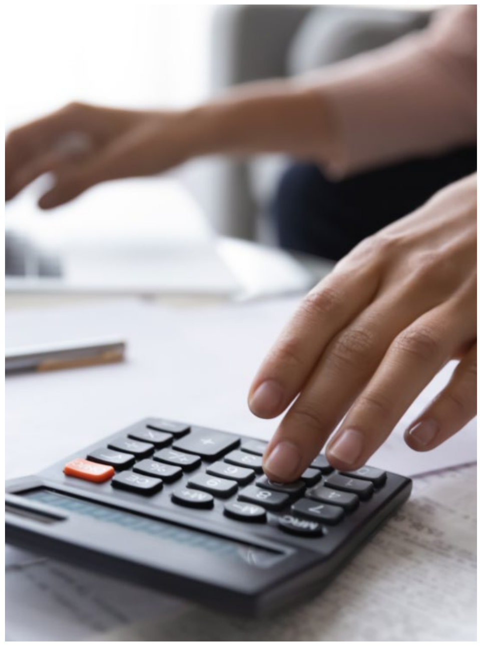
Unused Carry Forward = £35,000 - £20,000
= £15,000

*This example assumes that the member hasn't built up any other pension savings during the 2019/20 – 2021/22 tax years, nor were they subject to the 'tapered' annual allowance.

Most people won't be affected by the AA tax charge because the value of their pension savings won't increase in a tax year by more than the AA. If it does, they're likely to have unused allowance from previous tax years that can be carried forward to offset any excess.

How can I work out if I may be affected by the AA?

Working out whether you're affected by the AA is quite complex, but this should help you work out your general position.



In general terms, the increase in the value of your pension savings in a year is calculated by working out the value of your benefits immediately before the start of the tax year (6 April) and revaluing them by inflation (currently using higher of Consumer Prices Index (CPI) or 0%). This figure is then compared with the value of your benefits at the end of the tax year (i.e. the following 5 April).

In a defined benefit scheme like the LGPS, the value of your benefits is calculated by multiplying the amount of your pension by 16 and adding any separate lump sum you're automatically entitled to from the pension scheme.

If the difference between:

a) The value of your benefits immediately before the start of the tax year + CPI (the opening value);

and

b) The value of your benefits at the end of the tax year (the closing value) including any contributions you've paid into the EAPFs in-house Additional Voluntary Contribution (AVC) arrangement in the year

is more than the AA, you may have to pay a tax charge. The method of valuing benefits in other schemes may be different to the method used in the LGPS.

What happens if I transfer a previous pension into the EAPF?

If you elect to transfer pension rights into the LGPS from a public service pension scheme that takes part in the public sector transfer 'club', then any increase in benefits as a result of the transfer being calculated under 'club' terms counts towards your pension savings in the LGPS in the year the transfer payment is received.

In addition, if you combine any previous LGPS benefits with your current EAPF service, then any increase in value to your earlier benefits will count towards your pension savings.

Please note that the pension you're credited with following a transfer in from a private sector scheme (such as an insurance company, or a previous occupational pension scheme that isn't a public service pension scheme) doesn't count towards your pension savings in the LGPS in the year the transfer payment is received. The transfer amount will be included in your opening and closing values for the following tax year and will have a minimal effect on your pensions savings for that year.

What happens if I have a Pension Sharing Order following divorce or dissolution of a civil partnership?

If your pension benefits in the LGPS are reduced following a Pension Sharing Order (known as a 'pension debit') due to divorce or dissolution of a civil partnership, then for the purposes of calculating the value of your pension savings in the LGPS, the reduction in your benefits is ignored in the year that the Pension Sharing Order is applied to your benefits.

Vice versa, if, following a Pension Sharing Order, your benefits are increased (as a separate entitlement known as a 'pension credit'), the increase in your benefits is ignored in the year that the Pension Sharing Order is implemented.

What happens if I retire due to permanent ill health?

If you retire on the grounds of permanent ill health and an independent registered medical practitioner certifies that it's unlikely, you'll be able to work (in any capacity) before your state pension age, there's no AA tax charge on the ill health retirement benefits, even if your benefits are enhanced.

You're most likely to be affected by the AA tax charge if you:

- Have a lot of scheme membership that's linked to final salary and you've had a significant pay increase
- Pay high levels of AVCs or additional pension contributions (APCs), or have been awarded a lot of additional pension in the LGPS by your employer
- Transferred a pension into the EAPF from another public service pension scheme that takes part in the public sector transfer 'club' and your new salary is much higher than it was in your previous employment
- Combined previous LGPS final salary service with your current EAPF service and your new salary is much higher than it was in your previous employment.

We'll inform you automatically before 6 October, following the end of the relevant tax year, if your LGPS pension savings in that tax year were more than the AA.

We'll also tell you how much the value of your LGPS benefits have increased by and the amount of any AVCs you've paid during that tax year.

What happens if my pension savings increase by more than the AA?

If you exceed the AA in any year and you're unable to offset the whole of the excess against your carry forward of unused allowance, you're responsible for reporting this to HMRC on your self assessment tax return.

You'll also have to pay a tax charge (at your marginal rate) on any excess that can't be offset by your unused allowance.

If you have an AA tax charge, you may ask the EAPF to pay some, or all of the tax charge on your behalf; this option is called Scheme Pays. The tax charge would then be recovered as a deduction from your pension benefits.

Please note that you'll have the right to use Scheme Pays (known as Mandatory Scheme Pays) if you meet all of the conditions set out below:

- The AA tax charge is £2,000 or more;
- The AA tax charge is for pension savings above £60,000 in the LGPS alone; and

You elect for Scheme Pays no later than 31 July of the following tax year in which the AA charge relates (e.g. for a charge in the 2022/23 tax year, you must elect for scheme pays by 31 July 2024) However, if you're retiring and become entitled to all of your benefits from the LGPS and you want the EAPF to pay some or all of the tax charge on your behalf (with the relevant deduction being applied to your benefits), you must tell Capita (our administrators for the EAPF) before you become entitled to the payment of those benefits. Capita will be able to tell you more about this and the time limits that apply.

If you have an AA tax charge to pay, but you don't have the right to use Mandatory Scheme Pays, you may still elect for Scheme Pays, though only if the EAPF agrees to your request (if agreed, this is known as Voluntary Scheme Pays).

If this applies to you, you may apply in writing to Capita, giving the reasons for wanting to use Voluntary Scheme Pays.

If you need to contact Capita, you'll find their details at the end of this factsheet, or you can visit **www.eapf.org.uk/contact**

For more information on both Mandatory and Voluntary Scheme Pays, please see our 'Annual Allowance Scheme Pays – Questions & Answers' factsheet on our website at **www.eapf.org.uk/resources/publications**

You can also use our online 'Scheme Pays' tool at **www.eapf.org.uk/schemepays** to see how to apply.

Example showing the increase in pension savings for an active member of the LGPS throughout 2021/22

Working out the opening value of the member's benefits for 2021/22 - at 5 April 2021

Career average (CARE) pension built up to 31 March 2020	=	£7,200
Pensionable pay for the year 1 April 2020 to 31 March 2021	=	£60,000
Pensionable pay for the period 1 to 5 April 2021 (5 days)	=	£833
Pensionable pay for final salary benefits	=	£60,000

Scheme membership = 21 years & 5 days (8 years in the old 80ths scheme, 6 years in the 60ths scheme and 7 years & 5 days in the CARE scheme)

The career average pension is revalued by CPI; the CPI to apply for 1 April 2020 and 1 April 2021 is 1.7% & 0.5% respectively

The inflationary increase (determined by the Government) to apply to get the 'opening value' is 0.5%

			£
Annual pension	8 / 80 x £60,000	=	6,000.00
	6 / 60 x £60,000	=	6,000.00
	£7,200 + 1.7% +0.5%	=	7,359.01
	(£60,000 / 49) + 0.5%	=	1,230.61
	£833 / 49	=	17.00
Total annual pension			**20,606.62**
Multiply by 16			329,705.92
Add lump sum	8 x 3 / 80 x £60,000		18,000.00
			347,705.92
Inflationary increase			+ 0.5%
To give an opening value of			**349,444.45**

We don't include any AVCs paid in the opening value.

You'll see below how we work out the closing value of the member's benefits.

Working out the closing value of the member's benefits for 2021/22 - at 5 April 2022

Career average (CARE) pension built up to 31 March 2021	=	£8,546.89
Pensionable pay for the year 1 April 2021 to 31 March 2022	=	£61,000
Pensionable pay for the period 1 to 5 April 2022 (5 days)	=	£847
Pensionable pay for final salary benefits	=	£61,000

Scheme membership = 22 years & 5 days (8 years in the old 80ths scheme, 6 years in the 60ths scheme and 8 years & 5 days in the CARE scheme).

The career average pension is revalued by CPI; the CPI to apply for 1 April 2021 and 1 April 2022 is 0.5% & 3.1% respectively

AVCs paid between 6 April 2021 to 5 April 2022 = £1,000

			£
Annual pension	8 / 80 x £61,000	=	6,100.00
	6 / 60 x £61,000	=	6,100.00
	£8,546.89 + 0.5% + 3.1%	=	8,855.90
	(£61,000 / 49) + 3.1%	=	1,283.49
	£847 / 49	=	17.29

Total annual pension		**22,356.68**
Multiply by 16		357,706.88
Add lump sum	8 x 3 / 80 x £61,000	18,300.00
Add AVCs paid in this year		1,000.00
To give a closing value of		**377,006.88**

Working out the increase in value during 2021/22

The increase in the member's benefits over the year to 5 April 2017 is:

£377,006.88 - £349,444.45 = **£27,562.43**

This member has an annual allowance of £40,000 so there is no AA charge for this period, as the increase in the member's benefits is less than £40,000.

In addition, and assuming that the member hasn't contributed to another pension arrangement during 2021/22, they've £12,437.57 of unused AA from 2021/22 (£40,000 - £27,562.43) to carry forward to 2022/23.

Money purchase annual allowance (MPAA)

Although LGPS rules don't allow payment of money purchase AVCs before payment of main scheme benefits, it's possible to transfer the AVCs out of the scheme where they can be accessed flexibly.

If you choose to access your AVCs flexibly or any other pension savings in a money purchase arrangement, you'll trigger the MPAA. The MPAA, which came into effect from April 2015, has a limit of £10,000.

This reduced to £4,000, with effect from 6 April 2017 but increased again to £10,000 from 6 April 2023.If you exceed this limit by paying AVCs or contributions into another money purchase arrangement, then a tax charge will apply (unlike the AA, the MPAA excess can't be reduced by using any unused MPAA from previous years). Please note that the MPAA is included within your standard AA limit of £60,000.

Tapered annual allowance

Further reduction in the AA for high earners from April 2016

From 6 April 2016, changes to the AA rules introduced a 'tapered annual allowance' (TAA) that could affect people with a taxable income above the 'threshold income' (please see definition below).

Under the TAA rules, the standard AA reduces by £1 for every £2 of 'adjusted income' (please see the definition of 'adjusted income', below). If you've got adjusted income over £150,000 for any tax years between 2016/17 and 2019/20, adjusted income over £240,000 for any tax years between 2020/21 and 2022/23, or if you've got adjusted income over £260,000 for tax year 2023/24 onwards, your AA will be tapered and subject to the following minimum amounts.

Tax year(s) applicable	Threshold Income	Adjusted Income – tapering starts	Minimum Tapered Annual Allowance	Maximum Reduction in AA
2016/17 – 2019/20	£110,000	£150,000	£10,000	£30,000
2020/21 – 2022/23	£200,000	£240,000	£4,000	£36,000
2023/24 onwards	£200,000	£260,000	£10,000	£50,000

Definition of 'Threshold income'

'Threshold income', is broadly equal to your taxable income after the deduction of your total pension contributions (including any AVCs you've paid into the EAPFs in-house AVC) in a tax year.

Before 2020/21, if your threshold income was £110,000 or less, you wouldn't be subject to the TAA restriction, regardless of the level of your adjusted income. From 2020/21 onwards the threshold income limit rose to £200,000. Please note that anti-avoidance rules also apply.

Definition of 'Adjusted income'

In broad terms your 'adjusted income' is generally your threshold income plus the value of your pension savings.

If you exceed the standard AA we'll send you a pension savings statement which will tell you the value of the pension savings you made in the EAPF during the tax year that will count towards your adjusted income.

Lifetime allowance

What is the lifetime allowance?

The lifetime allowance (LTA) is the total capital value of all the pension benefits you can have without having to pay a tax charge when you draw them. If the value of your pension benefits when you draw them is more than the LTA, you'll have to pay tax on the excess benefits at your marginal rate of income tax.

The LTA covers any pension benefits you may have in all tax registered pension arrangements – not just the LGPS. However, this doesn't include any state retirement pension, state pension credit or any survivor's or dependant's pension you may be entitled to.

The current LTA for 2023/24 is £1,073,100, however the LTA is expected to be removed from legislation from 6 April 2024. Most people won't be affected by the LTA because they won't have pension savings of more than £1,073,100.

What happens if the value of my pension benefits is more than the LTA?

If the capital value of your EAPF retirement benefits is more than your remaining LTA you'll have to pay income tax on the excess. If your benefits exceed the LTA, the maximum available tax-free lump sum from the Scheme may also be restricted.

Prior to 6 April 2023, an LTA tax charge was applied at a rate of 25% for benefits in excess of the LTA taken as a pension, and at a rate of 55% in respect of benefits in excess of the LTA taken as a lump sum. However, the LTA tax charge was removed from legislation from 6 April 2023 and, instead, income tax at your marginal rate applies whether the excess benefits are taken as pension or as a lump sum.

You use up some of your LTA each time you start taking a pension on or after 6 April 2006.

How can I work out if my EAPF benefits could be affected by the LTA?

We work out the capital value of pension benefits that start after 5 April 2006, by taking your pension and multiplying it by 20, we then add on any lump sum you take on retirement. For example, if your yearly pension was £45,000 and you received a lump sum of £100,000 the capital value of these benefits would be £1 million i.e. (£45,000 x 20) + £100,000 = £1,000,000.

For pensions already in payment before 6 April 2006, the capital value of these pensions is calculated by multiplying the annual rate of the pension in payment at the time that you first start to draw other pension benefits after 5 April 2006 by 25. Any lump sum already paid is ignored in the valuation.

Each time you take a pension benefit, whether it is in the LGPS or another pension arrangement, you use up some of your LTA, so even if your pensions are small you should keep a record of the amount of LTA used up.

Are there any protections in respect of the LTA?

When the LTA was introduced from 6 April 2006, the two main protections for benefits built up to that date were Primary and Enhanced Protection. To be eligible for any of these protections you must have met the conditions required and registered with HMRC by 5 April 2009. If you already have Primary or Enhanced protection, you shouldn't be affected by a reduction in the LTA.

Reduction to LTA in 2012/13

When the LTA was first introduced, the limit was £1.8 million and when this reduced to £1.5 million in 2012/13, HMRC introduced an additional form of protection called Fixed Protection 2012 ('FP2012'). With FP2012, your LTA is fixed at £1.8 million or the standard LTA, if it rises to become higher than £1.8 million. You must've applied to HMRC before 6 April 2012 to have obtained FP2012.

You'll also be subject to restrictions on where and how you can transfer benefits. It's a condition of FP2012 that the amount of benefit you can build up will be limited, so if you have FP2012, and wish to keep it, you needed to stop your contributing membership before 6 April 2016.

If you lose FP2012, you must inform HMRC within 90 days.

Reduction to LTA in 2014/15

The LTA was further reduced to £1.25 million from 6 April 2014, resulting in further protections being introduced known as Fixed Protection 2014 ('FP2014') and Individual Protection 2014 ('IP2014'). FP2014 is similar to FP2012, and enabled you to fix your LTA up to a maximum of £1.5 million, meaning you can have pension savings up to £1.5 million without paying a tax charge.

You couldn't have FP2014 if you already have Primary, Enhanced or FP2012 and you must've applied to HMRC before 6 April 2014.

As well as holding FP2014, you may also hold IP2014. IP2014 has effect from 6 April 2014 for those who already had pension savings of over £1.25 million on 5 April 2014 and gives you a protected LTA up to a maximum of £1.5 million. You must've applied to HMRC before 6 April 2017 to have obtained IP2014.

Please note that you'll have lost FP2014 if you built up any benefits after 5 April 2016. If you lose FP2014, you must inform HMRC within 90 days.

Reduction to LTA in 2016/17

On 6 April 2016, the LTA was further reduced to £1 million, once again protections were introduced known as Fixed Protection 2016 ('FP2016') and Individual Protection 2016 ('IP2016'). The 2016 protections protect your personal LTA up to £1.25 million in the same way as the 2014 protections did. You can only apply for these protections online, however it is expected that there will be a final deadline of 5 April 2025 to apply for FP2016 or IP2016 in light of the removal of the LTA from legislation from 6 April 2024.

Please note that, you can't apply for FP2016 if you continued contributory membership after 5 April 2016 as you would not meet the requirements for keeping this protection.

Applying for Fixed and Individual Protection 2016

HMRC have introduced an online self-service for pension scheme members to apply for IP2016 or FP2016. Once you've successfully applied for protection, the online service will provide you with a reference number, which you'll need to keep and give to Capita.

Before applying you'll need:

- An account for HMRC online services - you can set one up when you start your application
- To know what your pension(s) were worth on 5 April 2016 and a breakdown of the amount

If you don't know this information, you can ask your pension scheme administrator. If you have more than one scheme, add the amounts from each scheme together.

For more information or to apply online, please visit www.gov.uk/guidance/pension-schemes-protect-your-lifetime-allowance

It's important to remember that most people will be able to save as much as they wish with full tax relief as their pension savings will be less than the annual and lifetime allowances.

More information

More information on the tax rules is available on HM Revenue and Customs website using the links below:

www.hmrc.gov.uk/pensionschemes/understanding-aa.htm
www.hmrc.gov.uk/pensionschemes/pension-savings-la.htm

General information on the Local Government Pension Scheme can be found at **www.eapf.org.uk** and **www.lgpsmember.org**

Contact details

If you have any questions regarding your pension entitlement you can contact our pension administrator, Capita, by:

Using the **'Ask us a question'** form on our website at **www.eapf.org.uk**

Emailing **info@eapf.org.uk**

Following on Twitter **@EAPensionFund**

Calling **0800 121 6593**
+44 114 452 5008 (overseas)

Sending your query to
Capita
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