"The text below consists of proposed amendments to the Registered Pension Schemes Manual, resulting from changes made by the Finance Bill 2008. As the Finance Bill has not yet received Royal Assent there can be no certainty about the final form of the legislation. The guidance is currently being developed in collaboration with customers in the Shared Workspace (RPSM public room) and may yet change. The text published here is work in progress. The final version of the guidance will be published after the Bill receives Royal Assent and will be in the form of changes to the Registered Pension Schemes Manual. This draft will then be withdrawn."

RPSM03104100 - Technical Pages: Protecting pension rights from tax charges: Enhanced protection: Cessation: Consequences

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Consequences of cessation

[Paras 12(3) & 49(2) Sch 36] [Reg 9 The Registered Pension Schemes (Enhanced Lifetime Allowance) Regulations – SI 2006/131]

An individual who has registered for enhanced protection will lose it if they do not comply with the conditions for enhanced protection.

Once enhanced protection ceases, **benefit crystallisation events** for the individual are potentially liable to the **lifetime allowance charge.**

The tax treatment, for the purposes of the lifetime allowance charge, of earlier benefit crystallisation events whilst enhanced protection was valid will not be re-visited when enhanced protection ceases.

If the individual had lump sum rights of more than £375,000 that included uncrystallised lump sum rights on 5 April 2006 on cessation of enhanced protection the individual will lose their lump sum protection. Unless another form of lump sum protection applies (see below) **pension commencement lump sums** should be paid under the normal rules described at RPSM09104100.

If the individual claimed primary protection as well as enhanced protection they will revert to primary protection once enhanced protection ceases. If on 5 April 2006 the individual had lump sum rights of more than £375,000 that included uncrystallised lump sum rights protection of lump sums as described at RPSM03105135 will apply.

Where primary protection was not claimed the individual will revert to the **standard lifetime allowance** once enhanced protection ceases.

If the individual

- had not claimed primary protection,
- had lump sum rights of more than £375,000 on 5 April 2006, and
- in any scheme on 5 April 2006 they had uncrystallised lump sum rights worth more than 25% of their total uncrystallised rights in that scheme,

the individual will revert to scheme specific lump sum protection as provided by paragraph 31 Schedule 36 (see RPSM03105510 to RPSM03105642 for more details).

At benefit crystallisation events after cessation of enhanced protection, the amount of the available lifetime allowance under section 219 Finance Act 2004 will be calculated in the usual way. (Benefit crystallisation events whilst enhanced protection was valid still use up the lifetime allowance.)

Where enhanced protection is lost, the individual also loses protection from the **annual allowance charge**. This will be from the start of the tax year in which enhanced protection is lost.

Glossary (RPSM20000000)

RPSM03105010 - Technical Pages: Protecting pension rights from tax charges: Lump sums: Introduction

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Introduction

For most members of **registered pension schemes** the lump sum rules after 5 April 2006 are at least as favourable as the rules that applied before that date.

However, there are some individuals whose lump sum rights will exceed £375,000 (25% of the **standard lifetime allowance** in 2006/07) on 5 April 2006. There will also be individuals whose lump sum rights exceed 25% of pension rights when the new system comes in. For all of these individuals, Schedule 36 of the Finance Act 2004 gives a degree of protection for their lump sum rights as they stood on 5 April 2006.

The way that the legislation protects lump sum rights exceeding £375,000 where primary or enhanced protection has been claimed is different from the way lump sum rights exceeding 25% of pension rights are protected. The chart on RPSM03105020 shows what type of lump sum protection an individual will be entitled to.

The different ways in which the legislation gives protection to the lump sum rights are dealt with in the following pages of this part of the guidance.

RPSM03105135 to RPSM03105182 details how protection of lump sum rights of more than £375,000 with primary protection works.

RPSM03105185 to RPSM03105230 details how protection of lump sum rights of more than £375,000 with enhanced protection works

RPSM03105500 to RPSM03105642 details how protection of uncrystallised lump sum rights of more than 25% works. This protection will not operate where an individual has total lump sum rights of more than £375,000 and they have claimed either enhanced or primary protection (or both).

Glossary (RPSM20000000)

RPSM03105500 - Technical Pages: Protecting pension rights from tax charges: Lump sums: Scheme specific protection: Contents

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Scheme specific protection of lump sum rights of more than 25% of uncrystallised pension rights: Contents

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RPSM03105515 - Technical Pages: Protecting pension rights from tax charges: Lump sums: Scheme specific protection: How it works

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How scheme specific protection of lump sum rights of more than 25% works

[Paras 31 – 34 Sch 36][Article 25 – 25D The Taxation of Pension Schemes (Transitional Provisions) Order 2006 – SI 2006/572]

The value of an individual's uncrystallised lump sum rights in a scheme on 5 April 2006 is identified. The legislation refers to these rights as VULSR.

The value of individuals uncrystallised pension rights in a scheme on 5 April 2006 is identified. The legislation refers to these rights as VUR.

RPSM03105530 to RPSM03105570 explain how VULSR and VUR are valued.

Where VULSR/VUR x 100 is more than 25 the legislation for the maximum **pension commencement lump sum** is rewritten to allow a scheme to pay a lump sum of more than 25%. Broadly the scheme will be able to pay a lump sum of the value of the allowable lump sum rights that were in the scheme on 5 April 2006 (revalued in line with the increase in the **standard lifetime allowance**) plus an additional lump sum amount (ALSA). RPSM03105580 gives more details.

Where on 5 April 2006 the individual was entitled to have all their benefits under all schemes relating to the same employment paid as a lump sum and they have had no relevant benefit accrual under the scheme (see RPSM03104080) all benefits may still be paid as a lump sum as long as certain conditions are met. This will not be a pension commencement lump sum but a **stand-alone lump sum**. RPSM03105640 explains when a stand-alone lump sum may be paid. If the conditions for a stand-alone lump sum are not met an individual may still qualify for a protected pension commencement lump sum.

Important points to note for pension commencement lump sum protection

This form of protection is specific to a particular pension scheme. If a transfer is made from the protected scheme lump sum protection may be reduced or lost. Further information can be found at RPSM03105521 and RPSM03105630.

A scheme receiving two or more **block transfers** in respect of an individual or a scheme already holding protected lump sums that receives a block transfer in respect of an individual can only protect one set of rights – see RPSM03105522.

This form of lump sum protection will be lost if certain conditions are not complied with – see RPSM03105520.

The legislation automatically provides this protection; there is no need for individuals to notify HMRC of this form of protection.

Although the legislation automatically protects individuals it does not compel schemes to provide the maximum lump sum.

The lump sum must still satisfy the usual requirement – see RPSM09104130 - that a pension commencement lump sum can only be paid when the individual becomes entitled to a relevant pension (unless the individual dies within 6 months of the payment and before becoming entitled to the relevant pension). In some cases an individual must be paid a pension commencement lump sum that is lower than the amount of the protected lump sum because part of their rights under the scheme must be paid as a pension. For example Andy has a protected lump sum of £100,000. The value of his crystallising benefits is £102,000. The rules of Andy's scheme require his pension to be secured by purchase of a lifetime annuity. The minimum annuity purchase price that can be found is £5000. So the maximum pension commencement lump sum that Andy can receive is £97,000.

Glossary (RPSM20000000)

RPSM03105520 - Technical Pages: Protecting pension rights from tax charges: Lump sum: Scheme specific protection: Conditions

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Protecting lump sum rights exceeding 25%: conditions

[Para 31(3) to (9) Sch 36] [Article 25 – 25D The Taxation of Pension Schemes (Transitional Provisions) Order 2006 – SI 2006/572 – as amended by The Taxation of Pension Schemes (Transitional Provisions)(Amendment No. 2) Order 2006 – SI 2006/2004]

For scheme specific protection under paragraphs 31 to 34 Schedule 36 FA 2004 to apply, three conditions must be satisfied

- the **registered pension scheme** from which benefits are paid must be either the scheme in which the rights were held on 5 April 2006 (the original scheme) or a registered pension scheme to which the rights were transferred as part of a block transfer or a registered pension scheme to which the final transfer in a series of block transfers has been made. The original scheme must be a **retirement benefit scheme** or a deferred annuity contract (section 32 policy) as defined at paragraph 1(1)(a) to (e) of Schedule 36 Finance Act 2004. A **block transfer** can be made to any registered pension scheme. RPSM03105521 gives more information on block transfers. RPSM03105630 explains what happens if a partial transfer is made from a protected scheme.
- the uncrystallised lump sum rights in the scheme on 5 April 2006 were more than 25% of the value of the uncrystallised pension rights in the scheme on that date, and
- the individual must become entitled to all of their pension and lump sum rights (that were not in payment on 5 April 2006) under the scheme on the same day. This condition will still be met where the individual dies within six months of the payment of the lump sum and before becoming entitled to the relevant pension.

Where the individual was entitled on 5 April 2006 to have all their benefits under all schemes relating to the same employment paid as a lump sum and they have had no relevant benefit accrual under the scheme (see RPSM03104080) all benefits may still be paid as a lump sum as long certain conditions are met. RPSM03105640 explains when all scheme benefits may be paid as a single lump sum.

The terms used to describe the uncrystallised lump sum rights and pension rights in paragraphs 31-34, Schedule 36, Finance Act 2004 are VULSR and VUR respectively.

Glossary (RPSM20000000)

RPSM03105521 - Technical Pages: Protecting pension rights from tax charges: Lump sums: Scheme specific protection: Transfers

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Transfers

[Para 31(7 - 9) Sch 36] [The Pension Schemes (Block Transfers) (Permitted Membership Period) Regulations 2006 – SI 2006/498]

When benefits are transferred from one scheme to another protection of lump sum rights of more than 25% will be lost unless the transfer is a **block transfer**.

Lump sum protection will be retained where an individual becomes a member of another **registered pension scheme** as a result of a block transfer. Where there is a block transfer the legislation treats the pension scheme receiving the block transfer as if it were the original protected pension scheme. Successive block transfers can be made without affecting the member's protection

A transfer is a block transfer if it involves the transfer in a single transaction of all the sums and assets representing accrued rights under the scheme from which the transfer is made which relate to the member and at least one other member of that pension scheme. To be a single transaction

- all of the sums and assets must be transferred from the transferring scheme to only one receiving scheme. Two or more partial transfers to two or more different schemes cannot be a transfer in a single transaction; and
- the transaction must be made under a single agreement for a single transfer between the two schemes.

It is not necessary that all of the sums and assets are all physically passed from the transferring scheme to the receiving scheme on the same day – there may be legal or administration reasons why this is not possible. However they should all be transferred in relation to the agreement to transfer and within a reasonable timescale.

There is no restriction on the type of registered pension scheme receiving the transfer. So a **personal pension scheme** can receive a block transfer as long as the other block transfer conditions are met.

Because of the nature of the scheme a **retirement annuity contract** and a deferred annuity contract (section 32 policy) cannot make a block transfer as there is only one member in the scheme. (Although see RPSM03106072 for an exception for deferred annuity contracts that were in existence on 5 April 2006. References to a protected pension age should be read as the right to a lump sum of more than 25%.)

Transferring rights for a member from one arrangement whilst retaining benefit rights in another arrangement in the scheme is a partial transfer and so cannot be block transfer. A partial transfer will reduce the amount of the protected lump sum in the transferring scheme – see RPSM03105630.

Before the transfer, the member must not have already been a **member** of the registered pension scheme to which the transfer was made for longer than 12 months before the date of the transfer. If the receiving scheme was approved as a **personal pension scheme** and the individual was a member on 5 April 2006 any period of membership is ignored where the member's rights before the transfer consist of only contracted out rights.

In this context a member includes not only **active members**, but also **deferred members**, **pensioner members** and **pension credit members**. For example if an individual is not an active member of the receiving scheme but is a deferred member (having deferred benefits held under the scheme) and has been a deferred member for more than 12 months before the transfer is made the transfer cannot be a block transfer.

Glossary (RPSM20000000)

RPSM03105580 - Technical Pages: Protecting pension rights from tax charges: Lump sums: Scheme specific protection: How to pay protected 25% plus lump sum benefits

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How to pay protected lump sum benefits exceeding 25%

[Para 34 Sch 36]

Where an individual does have lump sum rights that exceed 25% of their uncrystallised pension rights in a scheme, paragraph 34 Schedule 36 FA 2004 modifies paragraphs 2 and 3 of Schedule 29 FA 2004. The modification allows the payment of a **pension commencement lump sum** with a value greater than 25% of the combined value of the lump sum itself plus the value of the connected pension.

Lump sum not more than available lifetime allowance and no partial transfer out

Where the payment of the lump sum benefit will not use up all of the individual's available personal lifetime allowance (which may be greater than the **standard lifetime allowance)**, and there has been no partial transfer out in respect of the individual the amount of the lump sum payable as a pension commencement lump sum will be the amount of "VULSR" on 5 April 2006 increased in line with increases in the standard lifetime allowance plus an additional lump sum which relates to an increase in the value of benefits after 5 April 2006.

This amount is found by using the following formula

(VULSR x CSLA/FSLA) + ALSA

VULSR = the value of the individual's uncrystallised lump sum rights under the scheme on 5 April 2006)

CSLA = the standard lifetime allowance when benefit entitlement arises

FSLA = £1.5 million.

ALSA is the amount found by the formula

$$\frac{LS + AC - (VUR \times CSLA/FSLA)}{4}$$

LS = the amount of lump sum actually paid

AC = the amount actually crystallised by becoming entitled to a pension in connection with which the lump sum is paid. However where a **scheme pension** is paid from a **money purchase arrangement** AC will be the value of the scheme pension purchase price, i.e. the vale of the sums and assets made available to provide the scheme pension

VUR = the value of the individual's uncrystallised rights under the scheme on 5 April 2006.

RPSM03105530 to RPSM03105550 explain how the value of VULSR and VUR is obtained.

If the formula gives a negative result, ALSA will be nil and no further additional lump sum can be paid.

Finding the maximum allowable pension commencement lump sum is relatively simple for money purchase arrangements. RPSM03105590 to RPSM03105610 give examples.

Finding the maximum allowable pension commencement lump sum under a **defined benefits arrangement** that provides lump sum benefits by commutation is more complex - unless the scheme uses a lump sum commutation factor of 20:1. RPSM03105612 gives an example of paying a protected lump sum of more than 25% from a defined benefits arrangement.

Partial transfers reduce amount of lump sum

Where there has been a partial transfer out in respect of the individual the amount of the lump sum is adjusted to reflect the transfer out – see RPSM03105630.

Lump sum more than available lifetime allowance

Where the value of the proposed lump sum benefit is greater than the available amount of the individual's **lifetime allowance**, the proposed lump sum benefit should be calculated in the same way as described above. If all of the proposed lump sum benefit is paid, part of it will be subject to the **lifetime allowance charge** under section 214 Finance Act 2004 (see example in RPSM03105620).

No lifetime allowance available

Where the individual has already used all of their available personal lifetime allowance before becoming entitled to the lump sum, no pension commencement lump sum may be paid. Protection for the lump sum rights in the scheme has no effect.

100% lump sums

Where the individual has the right to take all their uncrystallised pension rights under all pension schemes relating to the same employment as a lump sum see RPSM03105640.

Glossary (RPSM20000000)

RPSM03105590 - Technical Pages: Protecting pension rights from tax charges: Lump sums: Scheme specific protection: Examples of payments

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How to pay protected lump sum benefits exceeding 25%: examples for money purchase arrangements where the member has not been an active member of the scheme after 5 April 2006

[Para 34 Sch 36]

Example 1

Ruth had a protected lump sum right of £50,000 in a **retirement benefit scheme** on 5 April 2006. The value of her total rights under the scheme was £100,000 on 5 April 2006. She left the employment relating to the scheme in 2005.

Ruth took her lump sum under the scheme in April 2016 when the **standard lifetime allowance** was £2.1 million. At this point the value of her rights under the scheme had risen to £138,000.

Ruth's lump sum rights in April 2016 are in principle made up of two elements, the revalorised amount of the lump sum rights as at 5 April 2006 and the ALSA lump sum. In her case the value of the ALSA lump sum is zero as the 38% increase in her rights under the scheme (FROM £100,000 TO £138,000) is less than the 40% increase in the value of the standard lifetime allowance (from £1.5 million to £2.1 million).

So Ruth could be paid a lump sum from the scheme of £70,000, calculated as

£50,000 x (£2.1 million/£1.5 million) + £0 = £70,000.

Example 2

The facts are the same as those for Example 1 above except that the value of Ruth's rights under the scheme in April 2016 is £160,000.

Now the ALSA lump sum has an actual value as scheme rights have increased by 60% compared to the 40% increase in the standard lifetime allowance. The amount of the ALSA lump sum will be £5,000 calculated as

(£75,000 + £85,000 - £140,000)/4

using the ALSA formula in RPSM03105580.

So in example 2 Ruth can be paid a lump sum from the scheme of £75,000, being £70,000 (the revalorised 5 April 20036 lump sum rights) plus £5,000 (the ALSA lump sum).

Glossary (RPSM20000000)

RPSM03105595 – Page Deleted

RPSM03105600 - Technical Pages: Protecting pension rights from tax charges: Lump sums: Scheme specific protection: Example payment – active member after 5 April 2006

How to pay protected lump sum benefits exceeding 25%: example for money purchase arrangements where the member has been an active member of the scheme after 5 April 2006

Fred has rights to a lump sum on 5 April 2006 of £50,000, and total pension rights valued at £100,000. The lump sum is payable by commuting pension rights.

Fred accrues further benefits under the scheme for another ten years, then takes all his benefits from the scheme on 6 April 2016. At this point, Fred's pension rights from the scheme, attributable to the whole of his pensionable service (before and after 5 April 2006), have a value of £220,000. Fred takes **unsecured pension** from the scheme.

Fred is entitled to a lump sum relating to benefits accrued both before 6 April 2006, and after 5 April 2006.

To calculate the maximum lump sum that can be paid, you need to calculate separately the lump sums that relate to the pre 5 April 2006 period and to the subsequent period.

By April 2016, the **standard lifetime allowance** has increased by 40% to £2.1 million as a result of indexation. To calculate the maximum pre 6 April 2006 lump sum, the rate of increase in the lifetime allowance is applied to Fred's pre 6 April 2006 lump sum. So Fred's pre 6 April 2006 lump sum right is now worth

£50,000 x (£2.1 million / £1.5 million) = £70,000.

The maximum post 5 April 2006 lump sum is 25% of the value of the increase in Fred's lump sum and pension benefits since 5 April 2006. Although Fred has pension rights of £220,000 in 2016, the increase from £100,000 in 2006 is not solely due to post 5 April 2006 benefit accrual. The post 5 April 2006 benefits are determined by subtracting the value of his rights on 5 April 2006, from the value of benefits paid by the scheme. The value of the rights on 5 April 2006 is the amount of VUR increased in line with the standard lifetime allowance to the date of payment. In this case, the benefit increase since 5 April 2006 is

£220,000 – [£100,000 x (£2.1 million/ £1.5 million)] = £80,000

So Fred can receive an ALSA lump sum of £20,000 (25% of £80,000) in respect of the increase in the value of his rights after 5 April 2006.

This means a lump sum of £ 90,000 may be paid (£70,000 plus £20,000) to Fred without incurring a tax charge.

This example is equally valid if Fred had purchased a **lifetime annuity** or had a **scheme pension** provided instead of taking unsecured pension from his **money purchase arrangement**.

Note if in this example Fred's rights under the scheme on 6 April 2016 had suffered an absolute decline in value from £100,000 to £95,000 the value of the additional lump sum amount (ALSA) will not be less than zero.

Glossary (RPSM20000000)

RPSM03105610 - Technical Pages: Protecting pension rights from tax charges: Lump sums: Scheme specific protection: Example payment - protected lump sum rights under more than 1 scheme

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Example of how to pay protected lump sum benefits exceeding 25% where the member has protected lump sum rights under more than one scheme relating to the same employment

Fred has total pension rights on 5 April 2006 of £100,000, split equally between two schemes. Fred has total lump sum rights of £50,000, again split equally between the two schemes.

He takes all his benefits from both schemes in 2011 when the **standard lifetime allowance** has increased by 20% to £1.8 million. In 2011, Fred had pension rights of £80,000 in Scheme 1 and £170,000 in Scheme 2. Fred was not an **active member** of Scheme 1 after 5 April 2006, but continued to accrue benefits in Scheme 2. He takes **unsecured pension** from both schemes.

Fred can receive lump sum benefits of £92,500 made up of

Scheme 1 - £35,000

Scheme 2 - £57,500

The Scheme 1 lump sum benefit is made up of

- £30,000 for the pre 6 April 2006 benefits (£25,000 lump sum right at 5 April 2006 increased by 20% - the increase in the standard lifetime allowance), plus
- £5,000 for the increase in the value of benefits after 5 April 2006 (being 25% of the increase in the benefits value after 5 April 2006). The increase in the value of benefits after 5 April 2006 is calculated as

  £80,000 – [£50,000 x (£1.8 million/£1.5 million)] = £20,000.

The Scheme 2 lump sum right is made up of

- £30,000 for the pre 6 April 2006 benefits (£25,000 lump sum right at 5 April 2006 indexed by the rate of increase in the standard lifetime allowance), plus
- £27,500 for the post 5 April 2006 benefit increase (being 25% of the benefit increase after 5 April 2006), calculated as

  £170,000 - [£50,000 x (£1.8 million/£1.5 million)], = £110,000.

This example is equally valid if Fred had purchased a **lifetime annuity** or had a **scheme pension** provided instead of taking unsecured pension from his **money purchase arrangement**.

Glossary (RPSM20000000)

RPSM03105612 - Technical Pages: Protecting pension rights from tax charges: Lump sums: Scheme specific protection: Example - defined benefit arrangement

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Example of payment from a defined benefits pension arrangement

On 5 April 2006 Helen has rights in a **defined benefits arrangement** of a pension of £10,000pa (uncrystallised value is £10,000 x 20 = £200,000) and a commuted lump sum right of £100,000. These benefits are within the HMRC maximum permitted pension and lump sum limits. So

VULSR = £100,000; VUR = £200,000

Helen's benefits come into payment on 1 July 2008 when the **standard lifetime allowance** is £1.65 million. By this time Helen's pension has increased to £21,000pa. The scheme uses a lump sum commutation factor of 12:1.

The pre 6 April 2006 rights have now increased as follows

VULSR = £100,000 x £1.65 million/ £1.5 million = £110,000

VUR = £200,000 x 1.65/1.5 = £220,000

To calculate the maximum allowable **pension commencement lump sum** Helen's **scheme administrator** has first to calculate the value of the ALSA lump sum. The total benefits crystallised will be

[Gross pension – (lump sum/ scheme commutation factor)] x 20 + lump sum

= [£21,000 – lump sum/12] x 20 + lump sum

= (£21,000 x 20) – (lump sum/12 x 20) + lump sum

= £420,000 – (20/12) lump sum + (12/12) lump sum

= £420,000 – 2/3 x lump sum

Total benefits crystallised = £420,000 – 2/3 x lump sum

The post 5 April 2006 increase in the value of benefits is [total benefits crystallised – VUR (revalorised]

= £420,000 – 2/3 x lump sum - £220,000

= £200,000 – 2/3 x lump sum

The maximum lump sum in respect of the post 5 April 2006 benefits (ALSA) is

LS + AC/4 (where LS + AC = £200,000 – 2/3 x lump sum)

= £200,000 x 0.25 – (2/3 x lump sum) x 0.25

= £50,000 – 1/6 x lump sum

The maximum lump sum = VULSR (revalorised) + the lump sum in respect of post 5/4/06 benefit increase (ALSA)

Lump sum = £110,000 + (£50,000 – 1/6 x lump sum)

Lump sum = £137,143

After taking this lump sum the crystallised value of residual pension will be

(£21,000 - £137,143/12) x 20 = £191,428

This result can be checked against the legislative formula

$$\text{VULSR x CSLA/FSLA} + \frac{\text{LS + AC – (VUR X CSLA/FSLA)}}{4}$$

= £110,000 + ({£137,143 + £191,428 - £220,000}/4)

= £110,000 + (£108,571/4)

= £110,000 + £27,143

= £137,143

Glossary (RPSM20000000)

RPSM03105630 - Technical Pages: Protecting pension rights from tax charges: Lump sums: Scheme specific protection: Partial transfer

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How to pay protected lump sum benefits exceeding 25% where there has been a partial transfer out of rights after 5 April 2006

[Para 34 Sch 36] [Articles 21 – 23 The Taxation of Pension Schemes (Transitional Provisions) Order 2006 – SI 2006/572]

This page is subject to change

Following enactment of Finance Bill 2008 consequential changes will be needed to the above named Order. This page is drafted on we anticipate the Order will be changed

Where an individual makes a partial transfer out of a protected pension scheme the amount of protected **pension commencement lump** sum is reduced.

The scheme the formula for payment is

[VULSR x (CSLA/FSLA)] + ALSA – TV/4

VULSR = the value of the individual's uncrystallised lump sum rights under the scheme on 5 April 2006)

CSLA = the **standard lifetime allowance** when benefit entitlement arises

FSLA = £1.5 million.

ALSA = the additional lump sum amount in respect of benefits accrued after 5 April 2006 (see RPSM03105580)

TV = the value of the sums and assets transferred out of the scheme after 5 April 2006.

In practice this means that ¼ of the transfer value is deducted from the usual amount of the protected lump sum (see RPSM03105580 to RPSM03105620).

RPSM03105635 gives some examples.

Where an individual's right under a protected pension scheme are reduced due to the transfer out of a **pension debit** the individual's protected lump sum rights remain unchanged.

Glossary (RPSM20000000)

New RPSM03105635 - Technical Pages: Protecting pension rights from tax charges: Lump sums: Scheme specific protection: Partial transfer - example

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Example of how to pay a lump sum exceeding 25% where there has been a partial transfer out of benefits after 5 April 2006

On 5 April 2006 Mark is a member of a pension scheme under which he has uncrystallised pension rights worth £60,000 and uncrystallised lump sum rights worth £30,000. This lump sum right of more than 25% receives protection.

In 2008 Mark transfers £40,000 out of this scheme to another pension **arrangement**.

In June 2010 Mark takes benefits from his protected pension scheme. When Mark takes benefits the value of his pension rights is £300,000. The **standard lifetime allowance** is £1.8 million. The maximum **pension commencement lump sum** that Mark can receive is £83,000.

This is amount consists of the revalued 5 April 2006 lump sum rights plus the amount of ALSA found using the formula in RPSM03105580 minus 25% of the £40,000 partial transfer.

The amount of the revalued 5 April 2006 lump sum rights is

£30,000 x £1.8 million/£1.5 million = £36,000

The ALSA amount is

{£300,000 – (£60,000 x £1.8 million/£1.5 million)}/4 = £57,000.

So the maximum lump sum calculation is

£36,000 + £57,000 – (£40,000/4) = £83,000.

Glossary (RPSM20000000)

RPSM03105650 – Page Deleted

RPSM03105660 – Text of page moved to become RPSM03105365

RPSM03201061 - Member Pages: Protecting pension rights from tax charges: Types of protection available: Amount of protected 25% plus lump sum

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The maximum lump sum that can be paid under scheme specific protection of lump sum rights of more than 25%

The maximum amount that can be paid is

- the value of your uncrystallised lump sum rights under the pension scheme on 5 April 2006 increased in line with the increase in the **standard lifetime allowance**, plus
- an additional lump sum amount (ALSA) that is broadly 25% of the value of the scheme funds that have increased above the rate of the increase in the standard lifetime allowance.

Example

On 5 April 2006, Jack has protected tax-free lump sum rights of £100,000 and his total pension rights are valued at £200,000. Jack's lump sum right under the scheme are worth 50% of his total benefits and as this is more than 25% he is entitled to scheme specific lump sum protection.

He continues as an **active member** of the scheme and on 12 June 2010 he takes all of his benefits from the scheme. His total pension rights from the scheme have now increased to £280,000, and the standard lifetime allowance has increased from £1.5 million to £1.8 million.

The scheme may pay a protected tax-free lump sum of up to £130,000 being made up of £120,000 in respect of the revalorised pre 6 April 2006 lump sum rights and £10,000 in respect of ALSA.

Pre 6 April lump sum rights are valued as £100,000 x 1.8/1.5 million = £120,000.

ALSA is calculated by first finding the value of the increase in the value of pension rights after 5 April 2006 and then taking 25% of the resulting value.

The increase in the value of pension rights after 5 April 2006 is calculated by subtracting the value of Jack's pension rights at 5 April 2006 (increased in line with the standard lifetime allowance) from the total value of benefits on 12 June 2010 - that is

£280,000 - (£200,000 x [£1.8 million ÷ £1.5 million) = £40,000.

The maximum amount of ALSA is £10,000 (£40,000 x 25%).

If on 5 April 2006 you had the right to take all your benefits under a scheme as a tax-free lump sum you may, provided certain conditions are met, continue to have this right. RPSM03105640 to RPSM03105642 set out when all your uncrystallised rights under a scheme may be taken as a lump sum.

Although the tax legislation automatically gives you this protection your pension scheme does not have to give you the maximum benefits. You may be given a smaller lump sum.

Glossary (RPSM20000000)

RPSM03304000 - Scheme Administrator Pages: Protecting pension rights from tax charges: Benefit payments - tax-free lump sum over 25%: Contents

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Benefit payments - tax-free lump sum in excess of 25% of the fund: Contents

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RPSM03304020 - Scheme Administrator Pages: Protecting pension rights from tax charges: Benefit payments - tax-free lump sum over 25%: Transfers out

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What should I do if a member's rights are transferred into another registered pension scheme?

Protection lost

If a member transfers all of their rights to another scheme after 5 April 2006, the protection of their lump sum benefit in excess of 25% is lost. The maximum **pension commencement lump sum** payable from the new scheme is then restricted to 25%, the amount allowable under the rules from 6 April 2006.

Exception for block transfers

If all of the member's pension rights are transferred to a new scheme as part of a **block transfer** (often when the company restructures its pension scheme or as a result of a take-over or merger) under the scheme, the member is still entitled to protection of their tax-free lump sum. RPSM03105521 tells you exactly what a block transfer is. However, broadly it requires more than one person transferring from the same pension scheme to the same pension scheme at the same time. If only one person in the scheme is transferring their benefits, it is not a block transfer.

In certain circumstances the purchase of a deferred annuity contract on the winding up of a pension scheme may be classed as a block transfer; see RPSM03106072 for the exact details.

The same rule applies if there is a subsequent block transfer after 5 April 2006. However you should note the contents of RPSM03105522 if it is intended to make a block transfer to a scheme where the individual already has a protected lump sum.

Exception for partial transfers

If a member transfers only part of their rights to another scheme after 5 April 2006 the rights being transferred out will not have lump sum protection under the receiving scheme. The rights remaining in the transferring scheme will still have protection of lump sum rights in excess of 25%. However the amount of the protected lump sum will be reduced by 25% of the value of the partial transfer out – see RPSM03105630.

Glossary (RPSM20000000)

RPSM03304050 - Scheme Administrator Pages: Protecting pension rights from tax charges: Benefit payments - tax-free lump sum over 25%: How much

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How is the tax-free lump sum calculated where the member does not have enhanced protection or primary protection with lump sum rights over£375,000 on 5 April 2006?

The member's maximum **pension commencement lump sum** is the value of the member's lump sum rights under the scheme on 5 April 2006 indexed in line with the increases in the **standard lifetime allowance** plus an additional lump sum amount (ALSA). The amount of ALSA is found by using the formula below.

$$\frac{LS + AC - (VUR \times CSLA/FSLA)}{4}$$

LS = the amount of lump sum actually paid.

AC = the amount actually crystallised by becoming entitled to a pension in connection with which the lump sum is paid. However where a **scheme pension** is paid from a **money purchase arrangement** AC will be the value f the scheme pension purchase price, i.e. the value of the sums and assets made available to provide the scheme pension.

VUR = the value of the individual's uncrystallised rights under the scheme on 5 April 2006.

CSLA = the standard lifetime allowance when benefit entitlement arises

FSLA = £1.5 million.

RPSM03304070 gives an example.

This amount can be paid provided that at the time the lump sum is paid the member has available **lifetime allowance**.

The amount of the maximum pension commencement lump sum is reduced if there has been a partial transfer out of the scheme in respect of the member – see RPSM03105630.

Where the member had the right to a 100% lump sum on 5 April 2006

Where the member's uncrystallised rights under a scheme on 5 April 2006 were either only lump sum rights, or the member could have taken all their rights as a lump sum, all the rights under the scheme may be paid as a **stand-alone lump sum**. This is only possible where on 5 April 2006 all the member's rights under all their retirement benefits schemes or deferred annuity contracts scheme relating to the same employment could have been paid out as a tax free lump sum without giving HMRC grounds for withdrawing scheme – see RPSM03105640.

RPSM03304100 gives more information about other payment conditions and rules relating to stand-alone lump sums.

If a member does not meet the conditions for a stand-alone lump sum they may still have a pension commencement lump sum of more than 25% if they continue to meet the conditions for scheme specific lump sum protection – see RPSM03304010. In these circumstances the limit on the lump sum is as described above and in RPSM03304070. However, a pension must also crystallise alongside the pension commencement lump sum.

Glossary (RPSM20000000)

RPSM03304060 – Page deleted

RPSM03304070 - Scheme Administrator Pages: Protecting pension rights from tax charges: Benefit payments - tax-free lump sum over 25%

How is the lump sum calculated?

The maximum amount of tax-free lump sum which can be paid from the scheme as a **pension commencement lump sum** is calculated in two stages.

First take the value of the member's protected tax-free lump sum rights under the scheme as at 5 April 2006 and index those rights in line with any increases in the amount of the **standard lifetime allowance** between 6 April 2006 and the tax year in which the benefits are being crystallised.

Second, the member may be entitled to an additional lump sum amount (ALSA). This amount is found by using the formula

$$\frac{LS + AC - (VUR \times CSLA/FSLA)}{4}$$

LS = the amount of lump sum actually paid.

AC = the amount actually crystallised by becoming entitled to a pension in connection with which the lump sum is paid. However where a **scheme pension** is paid from a **money purchase arrangement** AC will be the value f the scheme pension purchase price, i.e. the value of the sums and assets made available to provide the scheme pension.

VUR = the value of the individual's uncrystallised rights under the scheme on 5 April 2006.

CSLA = the standard lifetime allowance when benefit entitlement arises.

FSLA = £1.5 million.

These amounts when added together are the maximum amount of tax-free lump sum that can be paid from a scheme.

Example

On 5 April 2006, Jack has protected tax-free lump sum rights of £100,000 and his total pension rights are valued at £200,000. The standard lifetime allowance is £1.5 million in 2006-2007.

He continues as an **active member** of the scheme and on 12 June 2010 he takes all of his benefits from the scheme. His total pension rights from the scheme have now increased to £280,000, and the standard lifetime allowance has increased by 20% to £1.8 million.

The scheme may pay a protected tax-free lump sum of up to £130,000 being made up of £120,000 in respect of the revalued 5 April 2006 rights and £10,000 in respect of ALSA.

5 April 2006 rights are valued as £100,000 x 1.8/1.5 million = £120,000.

The portion of the lump sum in respect of ALSA is calculated by first finding the value of the pension rights accruing after that date and then taking 25% of the difference between the total value of the benefits on 12 June 2010 and the value of the 5 April 2006 rights increased in line with the standard lifetime allowance. That is

£280,000 - (£200,000 x [£1.8 million ÷ £1.5 million]) = £40,000.

25% of £40,000 is £10,000 .

The maximum total tax-free lump sum payable from the scheme on 12 June 2010 is therefore £130,000. However, the amount actually paid may be a lesser amount depending on the scheme rules.

Glossary (RPSM20000000)

RPSM03304080 - Scheme Administrator Pages: Protecting pension rights from tax charges: Benefit payments - tax-free lump sum over 25%: Benefits not increased above indexation amount

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What if the member's rights have not increased by more than indexation?

RPSM03304070 explains that the tax rules may allow the member to take an additional element to their **pension commencement lump sum** without incurring an **unauthorised payments charge**, based on the increase in the value of their pension rights after 5 April 2006.

However, if the value of the rights in the member's fund at the time of the benefit crystallisation event have not increased over and above the rise in indexation, no additional lump sum may be paid. (For example if the **standard lifetime allowance** increases by 20% by the date of the **benefit crystallisation event**, but the fund value only increases by 10%).

The member will however, still be entitled to take any indexed protected lump sum from the value of their rights as at 5 April 2006.

Glossary (RPSM20000000)

RPSM03304090 - Scheme Administrator Pages: Protecting pension rights from tax charges: Benefit payments - tax-free lump sum over 25%: Lump sum more than available lifetime allowance

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What if the member's lump sum is more than their available lifetime allowance?

Whether or not there is any or sufficient **lifetime allowance** left at the time entitlement to a lump sum arises depends on whether the member had already taken other pensions and lump sums prior to crystallising their protected lump sum.

If the member does have some available lifetime allowance but it is not enough to cover the whole lump sum, only part of it will be tax free. The part of the lump sum that is not covered by available lifetime allowance will be liable to the lifetime allowance charge and be taxed at 55%

Example

Sarah has protected tax-free lump sum benefits of £100,000, but her available personal lifetime allowance is only £50,000 at the time entitlement to her lump sum arises. The maximum lump sum payable tax-free from the scheme is £50,000. If the remaining £50,000 were to be paid as a lump sum although this would still be a pension commencement lump sum and it will taxable at 55% because it would be subject to the **lifetime allowance charge**.

If the member has no available lifetime allowance at the time entitlement to a lump sum arises the whole of the lump sum will be liable to a lifetime allowance charge at 55%. Such a lump sum will be a **pension commencement lump sum**.

What if the member has no available lifetime allowance when the lump sum is paid?

If a member has no available lifetime allowance when a lump sum is paid that lump sum cannot be a pension commencement lump sum. Members with transitionally protected lump sum rights must still satisfy the basic requirement that a pension commencement lump sum can only be paid when the member has available lifetime allowance.

Where a member has already used up their lifetime allowance any lump sum paid will be a **lifetime allowance excess lump sum** and thus liable to the lifetime allowance charge at 55% unless the member has enhanced protection. If the member has enhanced protection the lump sum will be an **unauthorised member payment** unless it is a **stand-alone lump sum** – see RPSM03304100.

Glossary (RPSM20000000)

RPSM03304100 - Scheme Administrator Pages: Protecting pension rights from tax charges: Benefit payments - tax-free lump sum over 25%: Stand-alone lump sum

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Payment of a stand-alone lump sum with scheme specific lump sum protection

Where on 5 April 2006 all an individual uncrystallised rights under all retirement benefits schemes or deferred annuity contracts relating to the same employment could have be taken as a tax free lump sum it may be possible for all the member's uncrystallised rights to be paid as a **stand-alone lump sum**. (RPSM03105640 gives more information.)

A stand-alone lump sum is the payment of all the member's uncrystallised rights under the scheme as a lump sum that is a single **benefit crystallisation event**.

A stand-alone lump sum can be paid once the member has reached the **normal minimum pension age** of 55 (50 until 5 April 2010) or any earlier protected pension age under the scheme. The lump sum can also be paid earlier if the member is taking benefits due to ill health – see RPSM08300080.

A stand alone lump sum cannot be paid

- if there has been relevant benefit accrual under the scheme,
- if the member has previously crystallised any benefits under the scheme (benefits paid before 6 April 2006 are ignored for this test), or
- once the member has reached age 75.

Transfers of benefits in respect of the member into or out of the scheme can also cause the member to lose their right to a stand-alone lump sum - see RPSM03105641.

Amount of stand-alone lump sum

Money purchase arrangements can pay a stand-alone lump sum which includes the full investment return on the value of the lump sum rights as at 5 April 2006 even though this is more than the 5 April 2006 value indexed in line with the **standard lifetime allowance**.

Defined benefits or **cash balance arrangements** can pay a stand-alone lump sum up to the amount of the appropriate limit. (RPSM03104525 explains what the appropriate limit is.)

The payment of a stand-alone lump sum is a benefit crystallisation event (BCE 6) so it is potentially liable to the lifetime allowance charge. Apart from the lifetime allowance charge it is not liable to income tax. So whilst the member has available lifetime allowance the stand-alone lump sum is tax-free.

RPSM03105642 gives an example.

Glossary (RPSM20000000)
