

Pensions: The Annual Allowance

Each year the Government sets the maximum level of tax-free contributions that can be paid into a pension and being in breach of the annual allowance can lead to some tough tax penalties.

The Annual Allowance

The maximum amount that can be contributed to a pension each year and which is eligible for tax relief is called the Annual Allowance. For 2023/24 this is £60,000 (previously, back to 2014/15, it was £40,000) which can be a combination of your own contributions and your employer contributions. To check whether you're reaching the annual allowance limit, you need to add up all your annual contributions **including** any tax relief added separately by HMRC. *(Remember that you only have one annual allowance, regardless of how many schemes you may have.)*



Simon Jackson Dip, PFS
Independent Financial Planner

Note: If you are in a defined benefit pension linked to your salary, the calculation is not as simple and you should ask your employer or pension scheme provider to check your position. We can also assist with this calculation.

Higher Earners

There are additional rules for those on higher incomes, as the Annual Allowance is 'tapered' for individuals with 'adjusted' income of more than £260,000 (£150,000 in 2016/17 to 2019/20, and £240,000 in 2020/21 to 2022/23).

Adjusted Income – refers to your entire taxable income for the tax year, i.e. your salary plus any additional income such as bonus, benefits in kind (P11ds), rental income, interest, dividends, etc, plus the value of any employer contributions (which includes any employer contributions as a result of a salary exchange arrangement).

Tapering - means that for every £2 of income over £260,000, the annual allowance is reduced by £1 up to a maximum reduction of £50,000*. Individuals will still have an Annual Allowance of at least £10,000* as illustrated in the table below:

| Adjusted Income | Annual Allowance |
|---------------------|------------------|
| Up to £260,000 | £60,000 |
| £270,000 | £55,000 |
| £300,000 | £40,000 |
| £360,000 or greater | £10,000 |

*maximum reduction of £36,000 so at least £4,000 Annual allowance in 2020/21 to 2022/23

Threshold Income

Individuals with lower salaries who may have one off spikes in their employer pension contributions will not normally be subject to the tapered Annual Allowance. Instead a threshold income of £200,000* (which excludes

pension contributions) will apply. However, anti-avoidance rules will also apply so that any salary sacrifice set up on or after 9 July 2015 will be included in the threshold definition. (**£110,000 in 2016/17 to 2019/20*)

The 'Carry Forward' Option

If you pay the maximum contribution for the current tax year, then you are able to carry forward any unused Annual Allowance from the 3 previous years. However, you must have been a member of a registered pension scheme in those years which you wish to carry forward.

If you have already taken an income from your pension using the new retirement flexibility rules introduced in April 2016, your Annual Allowance could already be restricted to £10,000 per annum and carry forward of unused Annual Allowance from the previous 3 years would not be available.

You *may* therefore be effected if

- a. your total income is greater than £260,000, and
- b. your total annual pension contributions exceed £10,000

Bear in mind that future wage increases could take you over the limit if you are already on a high salary.

Important Note – The maximum tax relievable contribution that an *individual* can pay to pensions each tax year is 100% of their relevant earnings or £3,600 whichever is the greater. This is subject to an overall maximum of the Annual Allowance together with any unused annual allowances from the previous 3 years.

Any contributions that exceed the annual allowance available will be required to be declared on your self-assessment tax return, and will be subject to income tax.

A Word of Caution

In some circumstances it may be worth continuing your pension contributions and paying the tax penalty anyway, for instance where your contributions are largely or entirely financed by your employer. However, you should seek professional advice and check all the implications carefully before taking any action.

There is clearly a lot to consider. For more information or assistance please get in touch with us on 01789 263257 or email us at justask@jjfsltd.com

Information in this document is valid for tax year 2023/24