

Scheme pays guide

Background

An annual allowance charge arises when any of the annual allowances are exceeded.

‘Scheme pays’ is a mechanism by which the annual allowance charge can be paid out of a pension scheme, rather than by the member personally. This has the advantage of the member not having to find additional funds to pay the charge.

There are four different annual allowances in place:

1	Annual allowance (AA) <ul style="list-style-type: none"> £60,000
2	Money purchase annual allowance (MPAA) <ul style="list-style-type: none"> £10,000
3	Tapered annual allowance (TAA) <ul style="list-style-type: none"> varies between £10,000 - £60,000 depending on income
4	Alternative annual allowance (AAA) <ul style="list-style-type: none"> varies between nil - £60,000 depending on income

The alternative annual allowance only applies to defined benefit pensions when the MPAA has been triggered and exceeded.

Those who have not flexibly accessed their pension benefits (i.e. have not triggered the MPAA) can still use carry-forward to reduce or eliminate any charge. If the MPAA has been triggered, then carry-forward can only be used in relation to defined benefit accrual.

Where can scheme pays be used?

Scheme pays can be used where:

- the annual allowance charge for the tax year exceeds £2,000, and
- the pension input amount for the pension scheme for the same tax year exceeds the annual allowance.

Scheme pays can only be used when the £60,000 annual allowance is exceeded.

In reference to scheme pays, it is the AA that must be exceeded, i.e. £60,000. If only the MPAA or TAA has been exceeded, then scheme pays cannot be used. However, it may still be possible to use ‘voluntary scheme pays’ instead – see following section.

For the scheme to be required to pay the charge the member must usually notify the scheme by 31 July in the tax year two years after the tax year to which the annual allowance charge relates. For example, for a charge relating to the 2024/25 tax year, the notification must be received by 31 July 2026. However, due to the McCloud ruling relating to public services pension reforms, the deadline is extended if the charge arises because of a retrospective change of facts. Where the member has received information from the scheme administrator about a change in the pension scheme input amount the deadline is extended to the earlier of 3 months after notification and 6 years after the end of the tax year concerned. This extension applies to all schemes if the conditions are met, not just public sector schemes.

The member cannot notify the scheme before the end of the tax year in which the charge arises except for when they intend to fully access their pension, or if they are approaching age 75 with unaccessed funds or funds in drawdown. In these cases, the notification must be received before the funds are accessed or age 75 is reached.

If the two conditions are met, and the scheme is notified before the deadlines stated above, then the scheme will become jointly liable with the member for paying the charge. Once the notification has been submitted, and if the conditions are met, then the member cannot withdraw the notice.

An important point to remember is that the annual allowance charge is not penal, it is simply reclaiming the tax relief that the individual is not entitled to above the annual allowance. Effectively this means that the excess pension contribution is not tax-relieved. It is important that higher and additional rate tax payers claim their higher/additional relief via self-assessment in the usual way, so the annual allowance charge offsets it.

Our process for scheme pays and voluntary scheme pays

If you would like to use scheme pays or voluntary scheme pays, please contact us for the appropriate form. In all cases we will require a copy of the member's self-assessment form including the pension savings tax charges section with details of the annual allowance excess, and the amount to be paid by the scheme.

If voluntary scheme pays is being used and contributions have been made into other pension schemes that have led to the annual allowance charge, a pension savings statement for the relevant tax year is required from those schemes. There is a charge for voluntary scheme pays as per our charges and rates.