AJBell Investcentre

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)** • £60,000
2	**Money purchase annual allowance (MPAA)** • £10,000
3	**Tapered annual allowance (TAA)** • varies between £10,000 - £60,000 depending on income
4	**Alternative annual allowance (AAA)** • 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 2023/24 tax year, the notification must be received by 31 July 2025. 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.

If the member has transferred benefits from the scheme into which benefits were accrued giving rise to the charge, and they would otherwise meet the conditions for scheme pays then they can no longer require the ceding scheme to pay the charge, but can instead require the new scheme to pay - providing the notification deadline is met.

Voluntary scheme pays

When the conditions for scheme pays are not met, then a scheme may pay the member's annual allowance charge on a voluntary basis.

This means voluntary scheme pays can be used to pay charges arising from exceeding the MPAA or TAA whether or not the AA is exceeded. It can also be paid from a scheme other than that which received the contributions relating to the charge. For example, a higher earner in a defined benefit scheme may exceed their tapered annual allowance due to benefit accrual in that scheme, but could have the charge paid on a voluntary basis from a SIPP or Retirement Investment Account they also hold.

Voluntary scheme pays can be used to pay any annual allowance charge.

As the name suggests, schemes do not have to offer this facility and they do not become jointly liable for the charge. As the liability remains with the member, the payment made by the scheme under voluntary scheme pays should be paid by the member's normal self-assessment deadline, i.e. 31 January in the tax year following that in which the charge arose.

To ensure that this deadline is met, the scheme will need to account for the tax charge in quarter 3 which runs from 1 July to 30 September. The tax for this period is paid to HMRC by 14 November. If the request is received in quarter 4 (1 October to 31 December), this tax is only due to HMRC by 14 February, so the 31 January deadline is unlikely to be met.

The scheme can still pay the charge on a voluntary basis at a later date but there is a risk the member may receive late payment interest charge, current rates for which can be found here – HMRC interest rates for late and early payments - GOV.UK (www.gov.uk). In practice, this charge has not always been applied when the self-assessment has stated that the scheme will be paying, but this cannot be guaranteed.

In order to pay an annual allowance charge under the voluntary rules, the scheme will need confirmation of pension input amounts to other schemes (if applicable), the amount of the charge, and the amount the member wants the scheme to pay. It is possible for the member to pay some of the charge personally, and some from the scheme.

Completing the self-assessment tax return

Anyone who has exceeded any of the annual allowances is required to report this to HMRC by completing a self-assessment tax return, even if they have not previously completed a return. They will need to complete the 'Additional Information' pages of the tax return (pages SA101 in the paper return). The boxes that need to be completed are in the 'Pensions Savings Tax Charges' section.

Pension Savings Tax Charges

7 Value of pension benefits in excess of your Available Lifetime Allowance, taken by you as a lump sum
£ . 0 0

8 Value of pension benefits in excess of your Available Lifetime Allowance, not taken as a lump sum
£ . 0 0

9 Lifetime Allowance tax paid by your pension scheme
£ . 0 0

10 Amount saved towards your pension, in the period covered by this tax return, in excess of the Annual Allowance
£ . 0 0

11 Annual Allowance tax paid or payable by your pension scheme
£ . 0 0

11.1 Value of pension benefits transferred subject to the overseas transfer charge
£ . 0 0

11.2 Tax paid by your pension scheme on your overseas transfer charge
£ . 0 0

In box 11 you should enter the amount that the scheme has paid, or will pay, under either scheme pays or voluntary scheme pays.

HMRC has produced guidance on completing the 'Pension Savings Tax Charges' section, and a working sheet to calculate the amount of the charge. Both these documents can be found here: HS345 Pension savings - tax charges (2021) - GOV.UK (www.gov.uk)

The annual allowance charge is calculated by adding the amount of excess pension savings to income for the year, then Income Tax is payable at the appropriate rate, which may be across different tax brackets.

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.

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