CARTWRIGHT

# REMOVAL OF THE LIFETIME ALLOWANCE

## What it means for Group Life benefits

## Background

Back in March, we gave our initial reaction to the Chancellor's decision to remove the Lifetime Allowance charge in April 2023. We also discussed his plan to eventually abolish the £1,073,100 Lifetime Allowance completely in 2024; subject to a Finance Bill going through parliament.

This paper discusses what this means for the Group Risk industry, notably Excepted Group Life schemes.

## What is the Lifetime Allowance?

People who have accumulated pension savings or a 'Pension Pot' over their lifetime will have received tax relief on pension contributions when paying into a scheme. As well as a pension, any proceeds from a Life Assurance Policy would also be exempt from tax.

However, to ensure high earners were not putting all their money into a pension for tax avoidance, the government placed a cap on the amount someone could pay into this over their lifetime. This cap was called the 'Lifetime Allowance'. It applied to both employer and personal pension contributions as well as the value of defined benefit pensions but did not include the value of the state pension.

After some significant reductions to the Lifetime Allowance, it finally stood at £1,073,100. These reductions had already begun to impact people who had a sizeable pension pot in the form of a Defined Benefit pension despite having a relatively moderate income.

## What impact does this have on Excepted schemes?

Lump sum death benefits, under employee benefit schemes, are typically written under a HMRC Registered Group Life Trust and are governed under Pensions legislation.

When combining the value of any Lump Sum Death Benefits and the value of Registered pension schemes, the Defined Benefit Lump Sum is normally paid tax-free up to the Lifetime Allowance. Prior to 6 April 2023, the excess over the lifetime allowance was taxed at 55% if it was taken as a lump sum.

Excepted Group Life schemes however are written under an Excepted Trust deed. They work differently in that they are governed under Life insurance legislation rather than Pensions legislation. As a result, the Lifetime Allowance does not affect these policies. What therefore happened until now was anything above the Lifetime Allowance was dealt with by setting up an Excepted Life policy to avoid any charges. In more recent years, some trustees have opted to place all Group Life benefits into Excepted schemes for ease of administration and to ensure any people who were bordering the Lifetime Allowance were captured.

Excepted Schemes have not be wholly adopted by the market because they do come with their own limitations. For example, any variance to a benefit calculation such as a change to a benefit basis or scheme salary definition, would require an additional policy to be set up. In addition, an exit charge may apply if there is a member with a terminal illness at the 10 year anniversary date.

The main purpose of an Excepted scheme should not be tax avoidance. However the announcement by the chancellor to remove the Lifetime Allowance charge, which was a large advantage of having an Excepted scheme now negates the need for an Excepted scheme(s). There may now be the argument to review whether an Excepted scheme of this type is now the most appropriate arrangement.

There are 10.6 million insured Group Life Assurance members of which, a substantial portion are set up under Excepted Life schemes. Of those, it is likely a reasonable portion, who had previously opted out of pension related schemes, may wish to opt back in. For Trustees this could be a significant exercise if they allow their members to do so.

Although any cessation/switching of Excepted schemes are likely to be carried out at the next rate expiry, there may be trustees who wish to carry out such a change sooner.

Group Life schemes which have an Excepted Life policy, on top of a Registered arrangement have to pay an additional policy administration fee by the insurer. They are often linked so they benefit from having a higher Unit Rate and Free Cover Limit for both policies. This fee is usually around £1,000 and is included within the insurer's premium.

For a large scheme, this would have minimal impact. The large premiums would likely swallow up any impact an administration fee may have on the rate. However for smaller schemes, the removal of any additional policy administration fees may be more noticeable, as £1,000 may represent a larger proportion of a premium. In those instances, there may be a wish amongst trustees to review their arrangements earlier.

## What next?

Draft legislation was published on 23 March 2023. However, the final wording will not be known until it passes through parliament. There is some hesitation within the market to act too hastily as the final bill is yet to be passed.

In addition, the impending General Election expected next year could potentially result in a new government; so legislation could change once again. Much will depend on the reaction to these changes by the insurance market and the insurance companies that provide Excepted policies.

Once a bill is passed, this will give greater foresight and certainty for the market to pave the way for concrete proposals. To monitor how the bill is progressing, you can follow using the link below: -

Finance (No. 2) Bill - Parliamentary Bills - UK Parliament

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