

# What are the tax-free lump sum allowances and how might they affect you?

## Tax-free lump sums

When taking pension benefits you normally have the option to take 25% of those benefits as a tax-free lump sum, with the remaining benefits (whether paid in pension or lump sum form) subject to income tax. Similarly, where a lump sum benefit is paid to your beneficiaries upon your death, those lump sums can also normally be paid tax-free.

## New allowances

From 6 April 2024, the total amount of your pension savings that can be paid as tax-free lump sums will be limited by two allowances: the **Lump Sum Allowance** and the **Lump Sum and Death Benefit Allowance**. Any lump sums in excess of the allowances will be subject to tax. Below we set out what each of these allowances are and how they may affect you. Some examples are provided on the next page.

*The note is based on the Finance Act 2024. Whilst we are aware HMRC intend to make some changes to the law in a few specific areas, our understanding is that they will not impact the content of this note.*

### Lump Sum Allowance

#### What is it?

The total amount of “retirement” tax-free lump sums you can take. For example, you may take one tax-free lump sum when you start drawing your final salary pension, or you may have a defined contribution pot and take several lump sums from it over a period of time. This allowance includes all of the tax-free element of your lump sum or sums.

**How much is it?** £268,275

#### What counts towards it?

- ✓ Pension Commencement Lump Sum
- ✓ The tax-free element of an Uncrystallised Funds Pension Lump Sum (ie 25% of the gross lump sum)

### Lump Sum and Death Benefit Allowance

#### What is it?

The total amount of tax-free lump sums payable on death or in cases of serious ill health; lump sums taken as part of the Lump Sum Allowance also use up this amount.

**How much is it?** £1,073,100

#### What counts towards it?

- ✓ Lump sum death benefits
- ✓ Serious ill health lump sum
- ✓ Pension Commencement Lump Sum
- ✓ The tax-free element of an Uncrystallised Funds Pension Lump Sum (ie 25% of the gross lump sum)

Payment of certain small lump sums or lump sums when a pension scheme is winding up do not use up either the **Lump Sum Allowance** or **Lump Sum and Death Benefit Allowance**. Your pension scheme will be able to confirm if this is the case.



## Examples

Here are some examples. They are given to illustrate how the allowances work – you should always seek professional advice if you are unsure of your own tax position.

### Kai

Kai has only a final salary defined benefit pension. He takes a pension of £15,000 a year (before tax), with a tax-free Pension Commencement Lump Sum of £80,000, reducing his remaining Lump Sum Allowance and Lump Sum and Death Benefit Allowance both by £80,000.

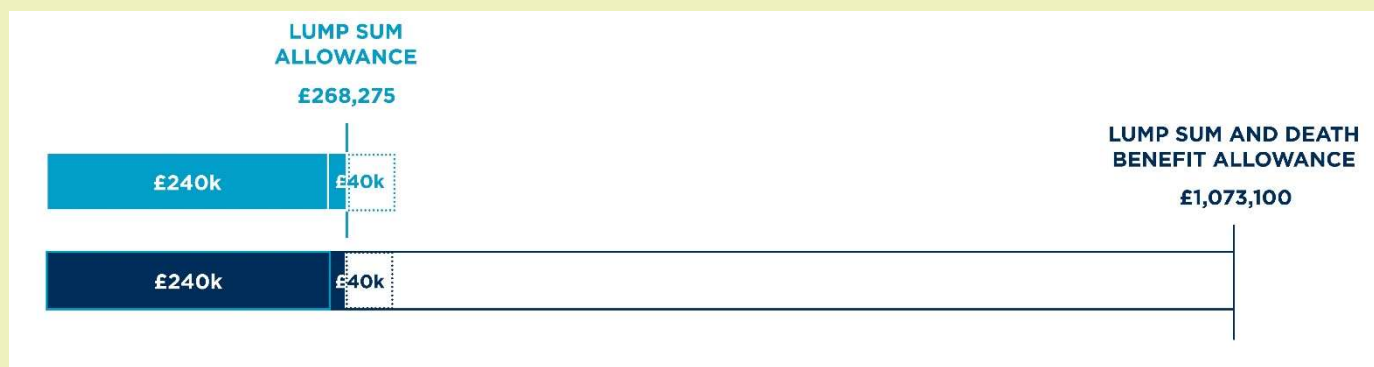
After taking his pension benefits, Kai dies. A lump sum is payable to his beneficiary of £68,000. The payment does not breach his Lump Sum and Death Benefit Allowance, so is payable tax-free.



### Maya

Maya has a final salary defined benefit pension and a defined contribution pension pot. She takes a final salary pension of £36,000 a year (before tax), with a tax-free Pension Commencement Lump Sum of £240,000; reducing both her remaining Lump Sum Allowance and Lump Sum and Death Benefit Allowance.

She also has £160,000 in a defined contribution pot. When accessing this pot a few years later, Maya would normally have the option of taking £40,000 (ie 25%) as a tax-free lump sum. However, she only has £28,275 of her Lump Sum Allowance left so the amount of lump sum that can be paid tax-free must be limited to that amount.



## Frequently asked questions

### What happens if I go over the Allowances?

If you breach the Lump Sum Allowance, you will pay income tax on any lump sums over the Allowance at your marginal rate. If the amount paid to your beneficiary breaches the Lump Sum and Death Benefit Allowance then *they* will be liable to pay tax on the excess amount at *their* marginal rate.

### What about the monthly pension I receive?

The tax-free allowances introduced in 2024 only include lump sum payments. Any benefits you take as pension will not count towards your allowances. Your pension will be subject to income tax.

### I drew some of my benefits before 6 April 2024, will my allowances reflect this?

Yes, if you drew benefits which used up some of your Lifetime Allowance, your allowances will be adjusted. For example, if you have previously used up 10% of your Lifetime Allowance, your two allowances will normally be reduced by 10% to reflect this. (If you can prove that you took a lower level of tax-free lump sum before 6 April 2024 you can make an application for the adjustment to reflect the actual lump sums taken, but such an application must be made before the first relevant lump sum is paid after 6 April 2024.)

### I have an existing protection – will this count for anything?

Some individuals with high levels of pension benefits may have an 'Individual' or 'Fixed' Protection granted by HMRC. If you have a Lifetime Allowance protection, your Lump Sum Allowance and Lump Sum and Death Benefit Allowance will be adjusted accordingly. For example, if you have a valid Fixed Protection 2014 certificate, your Lump Sum and Death Benefit Allowance will be £1,500,000 and your Lump Sum Allowance will be £375,000 (ie 25% of £1.5m). Similarly, if you have Individual Protection 2016 with a personal allowance of, say, £1,100,000 you will have a Lump Sum and Death Benefit Allowance equal to that value, and a Lump Sum Allowance of £275,000 (ie 25% of £1.1m).

In limited cases an individual may be entitled to a tax-free lump sum of more than 25%. This entitlement continues to apply, and their tax-free lump sum allowances will only be reduced by an amount representing 25%.

### Where can I find out more?

You can read more about pensions tax on MoneyHelper's website:  
[www.moneyhelper.org.uk/en/pensions-and-retirement/tax-and-pensions](https://www.moneyhelper.org.uk/en/pensions-and-retirement/tax-and-pensions).



Pensions tax can be complicated and you should consider whether to seek professional advice from a tax or financial adviser.

### Important information

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