



What is the annual allowance?

The annual allowance is a limit to the total amount of contributions that can be paid to [defined contribution](#) pension schemes and the total amount of benefits that you can build up in [defined benefit](#) pension scheme each year, for tax relief purposes. The annual allowance is currently capped at £40,000 although a lower limit of £10,000 may apply if you have already started drawing a pension. The annual allowance applies across all of the schemes you belong to, it's not a 'per scheme' limit and includes all of the contributions that you or your employer pay or anyone else who pays on your behalf.

If you exceed the allowance

If you exceed the annual allowance in a year, you won't receive tax relief -on any contributions you paid that exceed the limit and you will be faced with an annual allowance charge.

The annual allowance charge will be added to the rest of your taxable income for the tax year in question, when determining your tax liability. Alternatively, if the annual allowance charge is more than £2,000, you can ask your pension scheme to pay the charge from your benefits. This means your pension scheme benefits would be reduced.

Unless you have a money purchase annual allowance (MPAA), you may be able to bring forward any unused annual allowances from the previous three tax years, to either reduce your annual allowance charge to a lower amount or reduce the annual allowance charge completely.

Changes to the annual allowance

If you have taken flexible benefits which include income, such as an 'Uncrystallised Funds Pension Lump Sum (UFPLS)' or flexible drawdown with income, and you want to continue paying contributions to a defined contribution pension scheme, you will have a reduced annual allowance of £10,000 towards your defined contribution benefits. The reduced allowance will apply if you have withdrawn more than the 25% tax free pension commencement lump sum (PCLS). The reduced amount is known as the 'money purchase annual allowance (MPAA) and includes both your own contribution and any other contribution paid on your behalf, such as an employer or a third party. You cannot bring forward any unused annual allowances from the previous three tax years, to warrant a higher contribution of £10,000 towards your defined contribution benefits.

The money purchase annual allowance will only start to apply from the day after you have taken flexible benefits and so any previous savings are not affected.