

TAX-EFFICIENT PENSION PLANNING

*Helping you understand and make the most of your
pension provision and tax allowances.*

A close-up photograph of a person's hands using a blue calculator and a black keyboard on a wooden desk. The person is wearing a blue and white checkered shirt. A yellow cup is visible on the right side of the desk.

UNDERSTANDING HOW PENSIONS ARE TAXED

With the careful planning of allowances and exemptions, you could unlock your pension's potential to build up your wealth in a tax-efficient way and maximise your income at retirement.

Pensions are a very tax-efficient way in which to save money for your retirement, and in passing on wealth to future generations. One of the best features of using a pension to save for retirement is tax relief. When you pay into your pension, some of the money that would have gone to the government as tax, instead goes towards your pension and is given at the marginal rate of tax you pay.

Money you take from your pension pot comes from your provider with the tax already taken off, based on your tax code. Your provider may also take off any tax

due on your State Pension through Pay As You Earn (PAYE). On some occasions, you might pay emergency tax when you take money from your pot which you can claim back from HMRC.

However, whilst pensions offer many tax benefits, it is also important to be aware of certain allowances and thresholds in place - which we will discuss in this guide - and plan accordingly to avoid any penalties or additional charges whilst optimising your arrangements.

TAXATION ON PENSION CONTRIBUTIONS

How well do you understand how your pension contributions are taxed? There are different ways in which a pension can be taxed and there may be a more tax-efficient method than what your current pension is using.

Tax Relief

If you have income or capital available, consider contributing this into a pension to take advantage of the generous Income Tax relief available. The government will provide between 20%-45% Income Tax relief on your contributions, which can make a huge difference to your savings for retirement.

You may also have the ability to contribute via salary exchange (also known as salary sacrifice) which creates savings in National Insurance Contributions (NIC), therefore reducing the cost of paying into your pension.

Relief at Source vs Net Pay

There are two ways you can get tax relief on your pension contributions; relief at source and net pay. If you are in a Workplace Pension, your employer chooses which method is used. However, if you have a personal pension then the relief at source method is always used.

Looking at the example in the table across, whilst both methods would add £6 to the pension, with net pay the full £6 is taken from salary before income tax is calculated and you cannot claim any money back from HMRC. Whereas, with relief at source, only £4.80 is taken from their pay, and the rest of the £6 contribution is made up from tax relief (20% basic rate tax).

Method of Tax Relief Used	Net Pay	Relief at Source
Weekly/Annual Income	£200 pw (£10,400 pa)	£200 pw (£10,400 pa)
Contribution into Pension	3% (£6 pw)	3% (£6 pw)
Taken from Pay	£6.00	£4.80
Amount of Tax Relief	£0.00	£1.20

If you are a higher or additional rate taxpayer and make contributions via the Relief at Source method you need to claim extra tax relief not already claimed by your pension scheme, either through self-assessment or by contacting HMRC.

There are, however, certain limits that you need to be aware of which can impact the amount of tax relief you are entitled to, which is known as the Annual Allowance. Contributions in excess of these limits could lead to a tax charge on any excess relief provided.

Company owners can also make employer-based contributions into their pension plans. This can lead to lower Corporation Tax relief within their business, but any tax relief is subject to the discretion of the Local Inspector of Taxes.



PENSION ALLOWANCES

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