



## Making pension tax relief work for you

The idea behind tax relief is to encourage people to save for retirement. In allowing pension tax relief, the value of your savings for retirement are helped by money that would otherwise have gone to HMRC. This doesn't mean you won't have to pay tax on that money in the future, simply that you don't have to pay tax on it now.

### How much is tax relief worth to you?

Generally, the more tax you pay the more valuable tax relief will be to you. In summary, a £1 contribution today typically costs you 80p if you live in the UK and are a basic-rate taxpayer, as little as 60p if you're a higher-rate taxpayer and 55p if you pay additional-rate tax. Exactly how it works will depend on the way your pension scheme operates its tax relief. Rates of tax relief for Scottish Residents may differ to the rest of the UK.

The table below shows some worked examples based on different rate UK tax payers. The key thing to look at is the 'effective cost'. This is the overall cost to you to make the total contribution amount shown in the first column.

**Note** 'your total contribution amount' is not the amount you have to pay in, though in some cases it will be, but rather this is the amount that will be in the pension after the contribution has been made. The reason for this is that different pensions apply tax relief in different ways; we explain this on the next page.

### Other pension tax benefits

The tax relief on pension contributions comes on top of the other tax benefits available through pensions:

- The investments in your pension are sheltered from Income and Capital Gains Tax, which can make a significant difference to the value of your pension pot over the years.
- From the age of 55 you normally have the option of taking up to 25% (or sometimes more) of your pension as a tax-free lump sum. You are free to spend or invest this as you like, though you cannot reinvest it into another pension scheme.

The value of investments and the income from them can go down as well as up so you may get back less than you invest.

Your total contribution amount	Basic rate taxpayers 20%		Higher rate taxpayers 40%		Additional rate taxpayers 45%	
	Amount of tax relief up to	Effective cost as little as	Amount of tax relief up to	Effective cost as little as	Amount of tax relief up to	Effective cost as little as
£10,000	£2,000	£8,000	£4,000	£6,000	£4,500	£5,500
£40,000	£8,000	£32,000	£16,000	£24,000	£18,000	£22,000
£100,000	-	-	£40,000	£60,000	£45,000	£55,000
£130,000	-	-	£52,000	£78,000	£58,500	£71,500

These examples are not tailored to individual circumstances. All tax rules may change in future. Tax treatment (including the amount of tax relief you receive) and eligibility to invest in a pension depend on personal circumstances. You must pay sufficient tax at the higher or top rate to claim the full higher (40%) or top (45%) rate tax relief and to receive tax relief, your personal contributions can't be any higher than your earnings. Rates of tax relief for Scottish Residents may differ to the rest of the UK.

## How do I claim my tax relief?

This depends on how much you earn, what rate of Income Tax you pay and the type of pension you have. In many cases it's all handled by your pension provider. However, if you pay tax at a rate above the basic rate of 20% and have contributions going into a personal pension, you may need to claim any extra tax relief you're entitled to. Here's what you need to know:

### Personal pensions

Personal pensions, including self invested personal pensions (SIPPs), stakeholder pensions and those provided through the workplace like a group personal pension must use the 'relief at source' method. Here basic rate tax relief (currently 20%) is always applied to contributions that you or anybody other than an employer pay on your behalf. It is claimed by your pension provider and added to your pension pot. This means that if you only pay Income Tax at the basic rate or lower, including if you are not a taxpayer, you will not need to do anything else. So, if you made a personal contribution of £800 from your take home pay in to a personal pension, tax relief of 20% (currently) is applied automatically so the gross contribution in this example is £1,000. You can calculate the gross contribution amount you intend to pay by dividing the net contribution by 0.80 (100% - 20%). This is the amount that will appear in your account shortly after the contribution has been paid.

### Examples of tax relief if you're contributing to a personal pension



#### James stays at home to look after his children, no salary.

James receives an inheritance and pays £800 into his pension. Even though he doesn't pay Income Tax, James' pension contribution is topped up to £1,000 with tax relief. You can pay £2,880 into a pension plan and have it topped up to make a total contribution of £3,600.



#### Tim – engineer, salary £60,000.

Tim puts £800 of his overtime pay in a pension. Tim's contribution is topped up to £1,000 with basic rate tax relief, and because he earns enough to pay higher-rate Income Tax, he could then claim up to a further 20% tax relief. He gets a refund for £200 from HMRC so it has effectively cost him just £600 to put £1,000 in a pension.

Those that pay Income Tax above the basic rate, can potentially claim back more of the tax they have paid at those higher rates. For example, someone paying tax at the additional rate of 45% could claim up to 25% back, meaning up to £250 would be returned to them, bringing the cost of the pension contribution down as low as £550, though £1,000 remains in the pension.

You can claim the extra relief on your contributions through your tax return or simply by writing to HMRC with full details of your pension payments, plus your National Insurance number and taxpayer reference. Your claim can relate to contributions made as long as four years ago. Those that pay tax at more than the higher rate have to claim back through self-assessment. Income Tax rates for Scottish residents differ from the rest of the UK. However, if you pay more than the basic rate of income tax you can claim further tax relief in the same way. Individuals can only claim further tax relief against earnings that are taxed at higher rates.

### Workplace pensions

Some other workplace pensions, which are known as trust based plans, are usually dealt with slightly differently. They will typically use the 'net pay' method. In these schemes the pension contributions are taken from your pay before any tax is deducted - in other words they come out of your 'gross' pay. This means less of your income is taxed by the employer and you'll get full tax relief, unless you don't pay tax because you earn less than the starting rate for Income Tax. You will not need claim anything back from HMRC.

### Examples of tax relief if you're contributing to a trust based workplace pension



#### Cheryl – clerical worker, salary £20,000.

Cheryl receives a bonus of £1,000. She asks her employer to pay the money into her pension which her employer arranges. Because the money is paid straight into Cheryl's pension, she does not need to pay any tax on the money as nothing is being paid to her. She ends up with £1,000 in her pension and saves herself £200 in tax (which is the amount she would have paid once Income Tax at the basic rate of 20% had been applied before the bonus was paid to her).



#### Simone – project manager, salary £80,000.

Simone makes a one-off pension payment of £1,000. Her payment is not taxed so £1,000 goes straight into her pension. Because Simone earns enough to pay higher rate Income Tax, she benefits from tax relief of £400 (40% on the £1,000 she would ordinarily have paid tax on). Her pension has an extra £1,000 in it, but the overall cost to her is only £600.

**These examples are based on UK Tax Rates. The tax paid and relief given for Scottish Residents may be different.**

## How much can you pay in?

You are currently entitled to tax relief on pension contributions up to the total amount of your relevant earnings in a year, or £3,600 gross (£2,880 net), whichever is higher. However, there is an upper limit known as the annual allowance which is £40,000 for the 2019/20 tax year. Exceed this limit and a tax charge may become payable. This effectively claws back any excess tax relief given at source.

- So, if you earn £30,000, you could pay £24,000 into your pension and have it topped up by £6,000 to make a total contribution of £30,000, equal to the amount you earn.
- On the other hand, if your salary is £80,000, the most you could personally pay in to pensions in one year for tax relief purposes without making use of carry forward (see below for details) is £40,000. Remember this is the amount after tax relief has been applied. This means that if you are in a relief at source scheme (explained on page 2) you can contribute £32,000 which will have £8,000 of tax relief added, taking you up to the annual allowance of £40,000. As you'll be paying Income Tax at higher than the basic rate of Income Tax you could then claim further tax relief through your tax return.
- Even if you have no earnings at all, and therefore pay no tax, you can pay £2,880 into a pension plan and have it topped up to make a total contribution £3,600.

You should remember that the annual limit you can receive tax relief on for your pension contributions includes any contributions to a pension made by an employer. If you exceed the annual allowance across all your pension savings, not per scheme, you may have to pay a tax charge on the excess known as 'the annual allowance charge'. The rate of this annual allowance charge generally will be linked to the highest rate of Income Tax you pay. For more information on the annual allowance please speak to your adviser.

## Reduced allowance for high earners

For most people the annual allowance is usually £40,000 but for some higher earners i.e. those earning over £110,000 or more, this could reduce gradually from £40,000 to as low as £10,000 (for those who have 'adjusted income' of £210,000 or more). This is known as the tapered annual allowance. For more information and to see whether this affects you, your adviser will be able to help.

## Reduced allowance after withdrawals

Once you have taken taxable money out of your pension pot using pension freedoms (i.e. more than the tax-free part), your annual allowance may be reduced. This is known as the money purchase annual allowance (MPAA). You may also face restrictions on carrying forward unused allowances from previous years. Your adviser will be able to tell you whether you are affected by the MPAA.

## Make use of unused allowances to contribute more

If you have used up your annual allowance for the current tax year but want to contribute more to your pension and still benefit from the tax relief, you may be able to do so by using carry forward. Carry forward allows you to make use of any unused annual allowance from the three previous tax years.

You'll still need to have relevant earnings equivalent to the amount you want to contribute and other conditions may also apply.

## Lifetime allowance

There is also a lifetime allowance, designed to restrict the total amount anyone can build up in pension benefits over your lifetime that will enjoy full tax benefits. This is currently £1.055 million. Once the total value of all your pension savings (excluding your state pension) goes above this figure you will generally pay a tax charge on the excess when you take a lump sum or income from your pension pot, transfer overseas or reach age 75 with unused pension benefits. This is a complex area of pension tax law and you should consult your adviser if it could be an issue for you.

If you are unsure how tax relief works and how the annual allowances may relate to you, we suggest that you speak to your financial adviser or a tax specialist.

The information in this guide is correct as at 6 April 2019.

## What to do if you need help?

If you want to discuss your retirement options please speak to your financial adviser.