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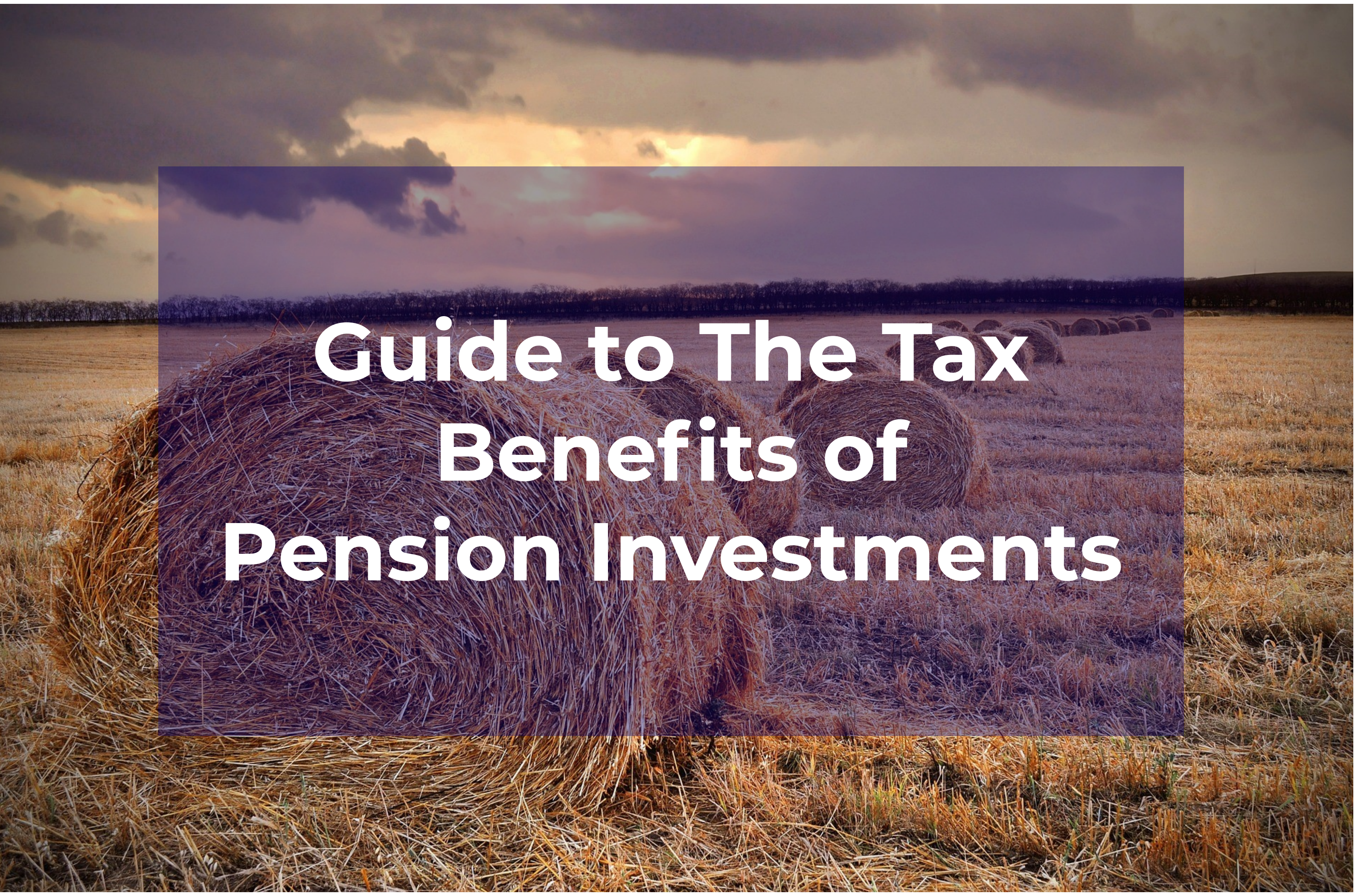
Investments • Pensions • Financial Planning



Guide to The Tax Benefits of Pension Investments

Background

Until April 2015 lack of access and high taxes on death could make pension funding unappealing, but under current rules, this has reversed.

Now, for anyone under age 75 so eligible for tax relief on a pension contribution, investing in a pension may be one of the best decisions they make in terms of tax planning.

However, it is important to stress that the Government has regularly changed the regulations applying to pension funds and might well do so again, so relying on current rules does, inevitably, involve some risk.

The tax benefits

With the above proviso, the current position is, broadly, as follows:

- Anybody under the age of 75 can enjoy tax relief on a pension contribution of at least £3,600 gross each year, and up to 100% of their gross earned income if higher. This is subject to a cap each year of between £10,000 and £60,000, depending on overall income levels and your pension withdrawal history.

- Basic rate tax relief is given “at source”, so a payment of £2,880 net has a tax credit of £720 added, to create £3,600 as a gross investment.

- For a high-rate taxpayer, additional tax relief is obtained through a claim to HM Revenue and Customs, normally via the self-assessment system.

- Up to 25% of a pension fund can be withdrawn free of taxes, subject to a cap of £268,275 (2024/2025).

- For those with estates at a size which could potentially give rise to an Inheritance Tax (IHT) liability, a pension fund might be a useful part of their estate planning. This is because a pension fund is normally exempt from Inheritance Tax.

- If a plan holder dies before age 75, their beneficiary can normally withdraw the fund, or an income from it, entirely tax free.

Other important tax points

- Withdrawals from a pension fund beyond the tax-free cash entitlement are normally treated as income for tax purposes, so taxed at the recipient's marginal rate, unless the fund has been inherited from someone who died before age 75.
- If taking a large withdrawal beyond the tax-free element this could cause a high-rate tax liability, so financial planning should be structured to avoid that situation.

Some possible drawbacks

While the advantages can be very attractive, the following issues should be considered:

- Unless a suitable pension plan is already in place there will be extra costs involved with establishing a plan to receive any contributions.
- The ongoing costs of operating a personal pension plan can be higher than the costs of operating, for instance, a stocks and shares ISA.
- If the Government changes the rules applying to pension funds it is possible that the current flexible access will be lost.
- If under age 55 (increasing to 57 from 6th April 2028), making a pension contribution will take away access to the capital until that age.
- Changes to the taxation of a pension fund could impact both the internal investments and the tax on withdrawal and these could make a pension less tax efficient than other options.

Conclusion and overview

- The relevance of the potential or actual benefits and drawbacks listed above will vary from one person to another.
- Based on the current rules, a pension contribution can be a very tax efficient way to invest, even for a basic rate taxpayer but exceptionally so for a high-rate taxpayer.

Important notes

The value of investments, other than deposit accounts or some guaranteed investments, will fall as well as rise, as can any income produced.

Any opinions expressed on the merits or disadvantages of any options are intended as a general comment only and not as specific advice to the reader.

This document is intended as a supplement to full independent advice and not as a replacement for it and should be read in conjunction with any personalised recommendations provided by Atkins Bland Ltd and with any product brochures supplied.

Any reference to taxation, regulation or legislation is based on our current understanding and details should be checked before any reliance is placed upon its accuracy

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Atkins Bland

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