



The benefits of pension investments

Why might a pension be worth considering as an investment vehicle?

A little background

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

Now, for anyone who is under age 75 and, therefore, able to obtain tax relief on a pension contribution, doing so may well 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.

Relying on current regulations to assess whether or not a pension investment will prove tax efficient does, therefore, 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 £3,600 gross as a minimum each year or at a figure of up to 100% of their gross earned income, whichever is higher. This is subject to a cap each year of between £4,000 and £40,000, depending on overall income levels and adjustments where certain types of pension withdrawals have already been taken.
- Basic rate tax of 20% is relieved at source and this means that anybody under the age of 75, even if they are not working, can make a contribution of £2,880 net and have this increased by a tax credit added to the pension to create £3,600 as a gross investment.
- For a high rate tax payer, additional tax relief is obtained through a claim to HM Revenue and Customs, normally via the self-assessment system.
- However, when the money is eventually withdrawn only 25% of it can be taken out as a tax free payment.
- The balance of the pension fund will be subjected to income tax at the recipient's marginal rate unless the fund is paid out as a consequence of the plan holder dying prior to age 75, in which case it will normally be paid to the beneficiary tax free.
- If someone has insufficient other income to use all their personal income tax allowance then it is possible that more than the 25% tax free lump sum entitlement can be withdrawn without giving rise to a tax liability.
- For those with estates at a size which could potentially give rise to an Inheritance Tax liability, a pension fund might be a useful part of their estate planning. This is because a pension fund is not normally taken into account for Inheritance Tax.

Other considerations

Some issues to be aware of when deciding if a pension is right for you

Possible drawbacks

While the advantages can be very attractive, the following issues do need to be taken into account:

- Unless a suitable personal pension plan is already in place there will be extra costs involved with
 establishing a plan to receive any contributions and these costs are likely to be higher than would
 apply if the money was invested elsewhere.
- The ongoing costs of operating a personal pension plan can be higher than the costs of operating, for instance, a stocks and shares ISA (although this is not always the case).
- If the Government changes the rules applying to pension funds it is possible that the current flexible access rules will be removed and money in a pension fund will no longer be available for withdrawal other than at prescribed limits per year.
- For somebody who is under aged 55, making a pension contribution will take away their access to the capital until they are at least 55.
- If a large withdrawal is needed in one tax year, this could cause someone who has always been a basic rate tax payer to pay high rate tax. Care needs to be taken to ensure other resources are available outside a pension if large scale withdrawals may be required at some point, beyond the 25% tax free cash entitlement.
- Changes to the taxation of a pension fund could impact both the internal investment and the tax on withdrawal and these could make a pension less tax efficient than other options. However, retrospective changes negatively impacting existing arrangements without allowing someone to exit the arrangement without adverse consequences seem unlikely as they would be manifestly unfair.

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 is a very tax efficient way to invest, even for a basic rate tax payer but potentially exceptionally so for a high rate tax payer.

However, there are some potential drawbacks. For some these will be more or less irrelevant but for others they may be pivotal.

If, on reading the above, you would like to consider making a pension contribution, please let us know.

Important notes

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.

The value of investments will fall as well as rise, as can any income produced.

Inflation can reduce the real value of capital and the income it generates

Past investment performance is not a reliable guide to the future

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.

The impact of taxation and tax planning depends on individual circumstances and may be subject to change, which can be retrospective.

Errors and omission excepted

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The value of investments and any income generated will fall as well as rise. An investor may, therefore, get back less than the amount invested.

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