eb@Shackletonadvisers.co.uk
www.shackletonadvisers.co.uk

Shackleton

Pensions Tax Relief Factsheet

For most people, pensions are usually a very efficient investment. This is because you receive Income Tax relief at your highest rate on money that you invest.

There are some limits on the amount of tax relief available – see Shackleton Employee Benefits Annual Allowance Factsheet.

If you need help in understanding the options available to you personally, or with collating contribution information for a tax relief claim, please contact Shackleton Employee Benefits.

There are three main ways in which individuals may contribute and receive tax relief:

Relief at source

Typically used by Personal Pensions including Group Personal Pensions and some large schemes such as NEST and The People's Pension.

Salary Sacrifice

Typically used by Personal Pensions including Group Personal Pensions and some large schemes such as NEST and The People's Pension.

'Net Pay Arrangements'

Typically used by 'occupational' pension schemes provided by larger employers.

Relief at source

All contributions are paid from Net Pay (after deduction of Income Tax and National Insurance). The pension provider automatically adds Basic Rate tax relief – so, an £80 net deduction from pay becomes a total contribution of £100 to the pension (Basic Rate tax currently being 20%).

This method of tax relief applies to any contributions that an individual pays directly to a pension provider as well as when employers deduct contributions from Net Pay.

Employees who pay Basic Rate tax have received all the Income Tax relief that they are due. Employees who pay higher rates of tax will have paid more than 20% Income Tax on the money invested in the pension and are therefore entitled to reclaim the difference directly from HMRC.

The table below shows the cost to employees at different Income Tax levels of a £100 gross contribution:

Tax Rate	Deduction from net pay	Extra Tax relief to be claimed	Total net cost to employee	Total contribution invested
20% Basic Rate (income less than £50,270 per year)	£80	NIL	£80	£100
40% Higher Rate (income between £50,270 - £125,140 per year)	£80	£20	£60	£100
45% Additional Rate (income over £125,140 per year)	£80	£25	£55	£100

As there is no automatic way for those that pay tax at a higher rate to receive their extra tax relief, they can only obtain this by claiming from HMRC. HMRC will also not be aware of any changes in the level of their contributions and they should thus confirm their total annual contributions each year. This may be done in a number of ways:

1. By telephone on 0300 200 3000
2. By post to PAYE and Self-Assessment, HMRC, BX9 1AS

   It should be made clear that these contributions are paid net of tax into a Personal Pension (not 'company pension' even though it is set up by an employer)
3. Via a Self-Assessment tax re-turn – the total gross contri-bution (the net amount paid plus the Basic Rate tax relief added) should be inserted into box 1 on page TR4 of the paper-based tax return:

Tax reliefs

Paying into registered pension schemes and overseas pension schemes

Do not include payments you make to your employer's pension scheme which are deducted from your pay before tax or payments made by your employer. If your contributions and other pension inputs are more than the Annual Allowance, you should also fill in boxes 10, 11 and 12 on page Ai 4 of the 'Additional information' pages.

1 **Payments to registered pension schemes where basic rate tax relief will be claimed by your pension provider (called 'relief at source'). Enter the payments and basic rate tax**

£ . 0 0

2 **Payments to a retirement annuity contract where basic rate tax relief will not be claimed by your provider**

£ . 0 0

3 **Payments to your employer's scheme which were not deducted from your pay before tax** – this will be unusual – read the notes

£ . 0 0

4 **Payments to an overseas pension scheme, which is not UK-registered, which are eligible for tax relief and were not deducted from your pay before tax**

£ . 0 0

If you submit your return online, then you will be prompted to state whether you paid into a pension and answering 'yes' will cause the above questions to appear.

Salary Sacrifice

Salary Sacrifice is an arrangement whereby an employee agrees to reduce their earnings in exchange for their employer paying an equivalent amount directly into their pension as an employer payment.

Using Salary Sacrifice means that the employee saves National Insurance Contributions (NICs) on the amount sacrificed. *Note that this will not apply to those older than State Pension age as they do not pay National Insurance.

It also has the additional advantage for employees in that no Higher or Additional Rate Income Tax relief need be claimed from HMRC as all their tax savings are made immediately. As the amount paid as a pension contribution is no longer deemed to be part of that individual's pay, then it is not subject to either personal Income Tax or NIC.

Individuals therefore receive immediate tax savings on the contribution with no need to inform HMRC.

The following table shows the cost to employees at different Income Tax levels of a £100 gross contribution:

Tax Rate	Deduction from net pay	Income Tax and NI saved	Total net cost to employee	Total contribution invested
Basic	£100	£20 + £8	£72	£100
Higher	£100	£40 + £2	£58	£100
Additional	£100	£45 + £2	£53	£100

'Net Pay Arrangements'

The term 'Net Pay Arrangement' can be misleading and is often confused with Relief at Source. A Net Pay arrangement is similar to Salary Sacrifice in that the contribution is deducted from an employee's **Gross Pay**, before tax. The taxable pay is lowered by the amount of their contributions which results in Income Tax savings at the highest rate that would otherwise have been paid had that money been kept as salary.

Unlike Salary Sacrifice however, there is no reduction in an employee's NICs.

PLEASE NOTE: with both 'Net Pay' and Salary Sacrifice, those whose earnings are under the tax threshold (£12,570) and who therefore do not pay Income Tax, would not receive any tax savings.
Those who do not pay Income Tax who contribute using Relief at Source would still qualify for Basic Rate tax relief even though they have not paid tax on their earnings.

Using pension contributions to reduce income below benefits or taxation thresholds.

As we've seen above, pension contributions can be very tax efficient. For people whose income is just above a threshold, pension contributions can have the result of not only gaining valuable tax relief, but also allowing someone to reclaim a benefit that they would otherwise have lost.

'Adjusted net income'

To understand how pension contributions affect your income level for tax and benefits purposes, we first must understand adjusted net income.

This is, broadly, taxable income (from all sources) less certain deductions, mainly pension contributions and 'gift aid' charitable contributions.

Adjusted net income is the figure that is used to determine your Income Tax rate and also the threshold used for some benefits entitlements.

Here's a simple Income Tax and NI table:

Income	Tax Rate	NI Rate	Total deductions
£0-12,570	0%	0%	nil
£12,570 - £50,270	20%	8%	28%
£50,270 - £125,140	40%	2%	42%
£125,140 +	45%	2%	47%

Other points to note:

- People over State Pension Age do not pay personal NI
- The tax-free Personal Allowance that applies to income up to £12,570 per year is lost on a sliding scale once total income exceeds £100,000.
  The Allowance is lost at a rate of £1 for every £2 of earnings above £100,000.
  The full Personal Allowance is therefore lost once total income reaches £125,140.
  This has the effect of taxing the income between £100,000 - £125,140 disproportionately: The effective rate of tax on this slice of income is 60%.

Example – income of £53,000

Using the table above, we can see that someone earning £53,000 would pay tax and NI totalling 42% on the top £2,730 of their income.

So, if they re-direct that income into a pension, they would receive tax relief of £1,092 on that money, effectively meaning that they paid no Higher Rate tax that year.

If they paid the contribution via Salary Sacrifice, then they'd also save NI of £54.60.

'High Income Child Benefit Tax Charge'.

Child Benefit is deemed to be taxable if either you or your partner earn over £60,000. You either must forego the Benefit or pay Income Tax on it.

So, by reducing their adjusted net income using pension contributions, individuals can not only invest very tax efficiently, but they may also now be able to receive Child Benefit (£1331.20 p.a. for the first child and £881.40 for any subsequent children).

The same process could also benefit people whose income is just over £100,000 – by reducing their adjusted net income via pension contributions, they can achieve effective tax relief on pensions of 60% and potentially also qualify for **Tax Free Childcare** that is normally lost once income exceeds £100,000.

As always, if you have any doubt about how any of these issues affect you as an individual, we recommend that you seek appropriate advice.

Useful links:

https://www.gov.uk/tax-free-childcare
Shackleton Employee Benefits Annual Allowance Factsheet

This document deals in generalisations, is intended for information purposes only, and is not intended to provide advice. Levels and bases of taxation will vary dependent upon individual circumstances and are subject to change. Shackleton recommend that employers and individuals take specific guidance before taking any action.

+44 (0)20 8125 4300

EB@Shackletonadvisers.co.uk

Unit 965, Cornforth Drive
Sittingbourne
Kent
ME9 8PX