



Factsheet: Pensions

Pensions are a great way to save towards retirement. The eventual size of your defined contribution pension pot is mainly determined by two things – the total contributions made and the performance of underlying investments.

You can choose to start taking your pension money once you reach age 55 (rising to 57 in 2028) to help fund your everyday life or you could not access it and pass it to your beneficiaries in an inheritance tax efficient manner.

Annual Allowance

The pension annual allowance is the total amount that you can contribute into a pension each tax year while also obtaining tax relief.

The standard annual allowance is £60,000 for the 2023/24 tax year however, if you have:

1. Less than £60,000 of relevant earnings
2. Adjusted income over £260,000
3. Accessed your pension benefits in a certain way

Then the standard allowance will be reduced from £60,000.

If an individual has exceeded their available annual allowance within a tax year, and the excess cannot be covered by carrying forward unused allowances from previous years, then there will be an annual allowance tax charge due on the excess. The charge is effectively clawback of the tax relief given in the first place rather than a penalty.

Relevant Earnings

Individuals are able to make contributions of up to the greater of £3,600 or 100% of their annual earnings to all of their pensions each tax year and receive tax relief on them.

In simple terms, 'relevant earnings' are self-employed profits and employment income (such as salary and bonus). It does however not include any rental income or dividends.

For example, if your salary is £20,000 then the amount you can put into a pension while obtaining tax relief would be £20,000 and not £60,000.

Tapered Annual Allowance

If you have a threshold income above £200,000 and an adjusted income of over £260,000 then your pension allowance will be reduced (tapered).

Calculating threshold income and adjusted income can be complicated. You should seek professional advice if your income is above £200,000.

For every £2 adjusted income that exceeds £260,000, £1 of pension annual allowance is lost down to a minimum tapered annual allowance of £10,000 which is reached if adjusted income is £360,000 or more.

Money Purchase Annual Allowance (MPAA)

When pensions are flexibly accessed under pension freedoms and you trigger the MPAA then the amount you can pay into a defined contribution pension may be reduced to £10,000.

There are many events that trigger the MPAA and many that don't. It is therefore important to seek advice before you take any capital from any pensions as some of the decisions you make could be irreversible.

Pension Carry Forward

If the annual allowance hasn't been used up in any of the previous 3 tax years, it may be possible to 'carry forward' the unused allowance. This can allow more to be paid in the current tax year.

But remember, the amount an individual can pay personally and receive tax relief on may be further limited by their relevant UK earnings. For example, you may have £80,000 that you can carry forward from previous tax years however, if your relevant earnings are £70,000, then this would be the amount you can contribute into a pension.

Lifetime Allowance (LTA)

The pension LTA is abolished from the 2023/24 tax year. The lifetime allowance was the maximum amount of pension savings that you can build up without incurring a tax charge when you retire which was at £1,073,100 in the 2022/23 tax year.

Protected Lifetime Allowance

Some individuals have protected lifetime allowances of £1.25 million, £1.5 million or £1.8 million which would be lost if they were to make a pension contribution into any pension.

If you have protected LTA, you can now make pension contributions without forgoing the enhanced tax-free cash and valuable protection benefits. Whilst there could be merit in making pension contributions, it would depend on your personal circumstances and financial objectives.

If you have protected LTA, we urge you to get in touch with an adviser.

Get in touch

We offer a no obligation first meeting to discuss your needs, goals and objectives.

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