

Financial Services Bulletin Tax Planning Strategies 2010/11 and beyond



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Guides & Advice

# Financial Services Bulletin

## Pension Contribution Tax Planning Strategies 2010/11 and beyond

If you are looking to maximise pension contributions then 5 April 2011 represents an important deadline and potentially the final opportunity to make a large contribution. In addition, there are actions you can take now which may increase the flexibility to make increased pension contributions in the future. In both cases, there is less than 5 weeks to take action.

It is worth first recapping on the main reasons funding a pension can be attractive:

- Up to 50% Income Tax relief on personal contributions
- Corporation Tax relief on employer contributions and no National Insurance due
- No Capital Gains Tax on growth and minimal Income Tax on income within the fund
- 25% tax free lump sum of accumulated fund at retirement
- Avoid 40% IHT – Likely tax free return of fund on death before retirement

With effect from 6 April 2011, the annual allowance (after which a tax charge is payable) is reducing to £50,000, a reduction of 80% from its current level of £255,000. In reality due to various changes in legislation, very few high income individuals can contribute more than £20,000 in the current tax year. However, there are exceptions and opportunities for tax planning specifically before tax year end:



- **Employer £255,000 Pension Contribution – Last Chance?**

2010/11 is the last year when a tax efficient employer contribution of £255,000 may be made. It is a frequent misconception that a pension contribution cannot exceed the level of income paid in any tax year (eg high dividend, low salary). In fact the employer can make significant employer pension contributions (up to £255,000 in 2010/11 and £50,000 beyond) in an extremely tax efficient manner. The main consideration is that the contribution passes the test of being “wholly and exclusively for the purposes of trade”. There are other factors to take into account such as how much relevant income the individual receives, but this does present an often overlooked opportunity, especially for business owners with significant cash within the business who want to release funds in a tax efficient manner

- **Personal £130,000 Pension Contribution Last Chance?**

2010/11 may be the last tax year when those with less than £130,000 “relevant income” (in any of tax years 2008/09, 2009/10 and 2010/11) can receive tax relief (up to 40%) on contributions over £50,000, without a tax charge.

- **Pension Scheme Membership – Join now pay later!**

If you are not in a position to make significant contributions this year but expect increased salary or profits in 2011/12 or subsequent tax years, ensure you are a member of a Registered Pension Scheme (that will accept future contributions) before the end of the 2010/11 tax year. If you are in a scheme before the end of the tax year and for example make a £10 contribution in 2010/11, in certain circumstances, you could make a contribution of £99,990 in the 2011/12 tax year and receive tax relief. Otherwise you could be restricted to a maximum of £50,000 for tax relief purposes in 2011/12.

- **Receive an effective 65% rate of tax relief on pension contributions**

For high earners, the personal allowance (the amount of tax free earnings) is reduced by £1 for every £2 earnings above £100,000. The personal allowance will therefore be eliminated at an income level of £112,950.

The effective rate of tax on income between £100,000 and £112,950 is therefore circa 60%. For an individual earning £112,950 a pension contribution of £12,950 will effectively receive tax relief at a rate of 60%. Should that individual also enter into a salary sacrifice arrangement with their employer, a further saving could be made leading to an effective tax relief rate of circa 65%. In such circumstances a £14,608 contribution could be made at a cost of £5,051 to the employee.

Of course whilst there are significant opportunities to make tax efficient contributions into pensions, each individual should have regard for their own circumstances. We would be happy to advise you as to the availability of this extremely valuable relief and the appropriate steps which should be taken.

This newsletter is intended for the use of clients and other interested parties. The information contained in it is believed to be correct at the date of publication but it is necessarily of a brief and general nature and should not be relied upon as a substitute for specific professional advice.

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