

Outside IR35 and no pension? Get tax savings with a pension

If you are contracting and don't have a pension, you are missing out on significant tax savings, even if you aren't caught by [IR35](#)?

Why? Because you can avoid lots of taxes by diverting your income into a pension. Here's how it works...

What can be saved?

If you are contracting outside IR35 you probably have a [limited company](#) and are paying yourself a [low salary](#) and the rest in [dividends](#). Because of your low salary, this meant in the past that you couldn't put more than £300 per month into a pension due to age related allowances. But everything changed for pensions funding since the so-called 'A Day' in April 2006 when the regime was vastly liberalised.

Contractors outside IR35 can now make company contributions to a pension of up to £50,000 per year, with a lifetime allowance of £1.8 million.

So, whilst there are no further N.I. tax savings with pensions (as for contractors inside IR35) there are still large savings to be made by avoiding corporation tax, and income tax, particularly for higher rate tax payers. Remember, any money invested in a pension goes in **before** these taxes are applied, offering significant 'tax relief'.

An example:

For a contractor outside IR35 earning £40 per hour, each £100 earned attracts £39 tax with only £61 ending up in their pocket.

Instead of drawing £100 as income the whole £100 could be contributed to a pension. This reduces net income by £61, but increases a pension by £100, attracting tax relief of 39%.

In the April 2010 Budget the new additional rate of income tax of 50% was introduced for those earning over £150,000. For those contractors earning more than £150,000 per year the tax relief is even higher. But for those earning just over £100,000 per year the effective tax rate is 60% due to the reduction in personal allowances introduced, resulting in tax relief even higher still. For high earners pensions are now an even more attractive option as a tax saving device for contractors than before.

You can calculate your own potential savings using the [Contractor Pension Calculator](#).

Some Quick Facts About Pensions

1. Pensions aren't all about saving money to buy an annuity. You can withdraw 25% of your pension funds tax-free from age 55. And rather than buying an annuity, you can continue to draw from the funds each year to maximum limits.
2. Your savings can be passed on to your family if you die before age 75 - provided you've not bought an annuity. The money will not be subject to inheritance tax.
3. You no longer pay large portions of your payments in commissions to an IFA - charges are negligible - comparable to buying a tracker fund.
4. Your funds are perfectly safe as pensions funds cannot become insolvent. A private pension fund is carefully protected by law.
5. If you're risk adverse and concerned about funds invested in the stock market you can option for keeping the pot in cash - just like an ISA.

Pensions are certainly no longer the rigid investments they used to be.

You can find out more by reading [Pensions for Contractors - An Overview](#).

Pension Quotation

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