

## Pensions for contractors with a limited company

If you have your own limited company, you can get very significant tax advantages through pensions while at the same time building up a fund which you can start withdrawing from starting at age 50 (or 55 for younger investors from April 2010).

### Pensions Are Liberalised

Everything has changed for pensions funding since the so-called 'A Day' in April 2006 when the regime was vastly liberalised.

### No Limits

"Apart from a small number of very high earners, in effect there are no longer any limits to contributions you can make from your limited company income into pension funds-- its safer that the amounts must not be larger than your corporate income for the year of the contribution, otherwise there might be questions from the Revenue about whether the money was actually sourced from your trading activities," explains Tony Harris, director of the Richmond, Surrey-based [ContractorFinancials](#), which offers independent financial advice and specialises in contractor affairs.

### 'Pre-Taxed' Income

Your [limited company](#) can contribute 'pre-taxed' company income to a pension. If you are a higher rate tax payer, instead of declaring the income as company profit and taking the income as a [dividend](#), you can put the sum straight into a pension.

### Dividends Versus Pensions

You can take a look at our [pensions calculator](#) to get a better idea for your own situation, but here's an example:

You have £100 worth of company income, and you are a higher rate tax payer, not caught by [IR35](#). You can either put the £100 into a pension, or you can declare it as profit and take it as a dividend.

But if you choose the latter option and take a dividend payment, you pay:

1. £21 in corporate tax on your £100, leaving £79
2. 22.5% personal income tax on the dividend, which takes another £17.78
3. Your total take home is £61.

Choosing the pensions option means that the whole £100 goes into a pension fund and then has an opportunity to grow in a tax efficient environment. In reality £25 of your contribution represents the part of the pension fund which you can draw tax free when you are retire. £36 of your money also goes into the pension fund, together with the £39 that would have gone to the taxman (quite a decent initial 'return' on your £36). This £75 can also grow and be used to skim off an income at a later date, or buy an annuity.

For contractors earning over £150,000 per year the tax saving is even more due to the new 50% tax rate introduced in the April 2010 Budget. And for those earning just over £100,000 per year the effective tax rate is 60% due to the reduction in personal allowances introduced. For high earners pensions are now an even more attractive option for tax savings than ever before.

### Annuities, Skimming, Inheritance

You don't have to buy an annuity until you reach the age of 75. Before that time you can skim a certain amount from your pension as income. Most annuities only pay around a 5% return, but remember you've only invested £36 yourself, but with the £39 from the taxman it is paying off as £75. So even with the choice of an annuity your overall return could be much higher because of the initial tax savings.

In the event that you die before you retire, if you've not taken an annuity, the whole of your fund can be passed on as an inheritance completely tax free.

Contractors should not fear that they are 'making a rigid commitment' to pension funding. "Any contractor pension should be flexible: as a contractor your employment status is inherently changeable and you must have complete freedom to increase, decrease, suspend, restart and cease contributions completely - literally on month by month basis," Harris points out.

“ There are no longer any limits to contributions you can make from your limited company income into pension funds; the amounts must simply not be very much larger than your actual declared corporate income ”

Tony Harris -  
ContractorFinancials


“ As a contractor your employment status is inherently changeable and you must have complete freedom to increase, decrease, suspend, restart and cease contributions ”

So whether you choose a pension with an eye to an annuity, or just to taking some tax-efficient income for yourself as you reach a more advanced age, you should not neglect this possibility for an entirely legal and risk-free tax-saving strategy.

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ContractorFinancials offer jargon free and timely mortgage, pension, insurance and investment solutions tailored to the unique needs of Contractors. [Read Full Profile...](#)

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