

Effective retirement planning for contractors

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For many contractors, especially to those new to the higher earnings and lifestyle advantages, retirement planning just is not on their radar.

Why worry when there is so much money coming in? But, according to [Angela James](#) of [Contractor Wealth](#), a financial advisor who specialises in contractor financial advice, cash rich times are exactly when retirement planning should begin.

"In addition to their big differences in flexibility and rates of pay," explains James, "contractors and permanent employees differ fundamentally in how their retirements are funded."

As she points out, most permanent employees in comparable roles to contractors traditionally have a company [pension](#) plan. Even employees who job-hop through various permanent roles and accrue a patchwork of different [pension schemes](#) are making some preparations for their future.

"Many employees are only vaguely aware of their company scheme, perhaps noticing payslip deductions every month and the occasional memo from the human resources department."

However, these pensions will generally give employees at least a comfortable retirement, without them having to give retirement planning much thought.

No benefits for contractors – or are there?

Contractors have to work at their retirement planning a bit harder, but the rewards can be very much greater. "Because they are not employees of their client, contractors don't receive any benefits as a result," says James. "However, many contractors are [contracting through their own limited companies](#), which allows them huge freedom in how they disburse the company's income."

Contractors who trade using a limited company generate fee income from clients into the company. The contractor then has a choice of how they disburse this income:

On costs incurred by the business, such as buying new computer hardware

As salary paid to employees – usually the contractor/company owner – including any Pay As You Earn (PAYE) income tax and National Insurance Contributions (NICs)

Through [dividends](#) paid to shareholders – again, usually the contractor/company owner – plus income tax on the dividends

As payments into a pension fund.

Spending cash in the business on expenses reduces the profits in the company and therefore the overall tax bill, saving the contractor money. Similarly, cash spent on pension contributions is a cost before tax, so the more a contractor pays into their pension, the lower their tax bill will be.

Umbrella companies and IR35

The situation for contractors using limited companies that are caught by [IR35](#), or those working through [contractor umbrella companies](#), is different, although both groups can still benefit from a flexible retirement planning approach.

"Contractors caught by IR35 can still make significant contributions to their pensions," continues James, "but as their outgoings will be greater – for example they will be paying income tax and both employee and employer NICs on a large part of their earnings – the amount they have to invest in retirement planning will be less."

James goes on to say: "It's also likely that contractors caught within IR35 on one contract may not be caught in another, and will have the opportunity to top-up their contributions."

Contractors working through umbrella companies have limited options to gain from significant overpayments, but are generally not restricted to a particular company scheme, so, as their career evolves and they move around, they can take their pensions with them.

Flexible timing

According to James, most company pension schemes are inflexible and the employee is destined to retire at a specified age, whether or not they want to.

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Angela James, Contractor Wealth

Contractors, however, can pretty much do what they like. "Contractors can choose to retire earlier, or later," says James, "and we have many clients working in their sixties because they want to, although they also have their retirement income for those times when they don't want to work."

Another valuable feature of contractor pensions is that if the contractor wants to reduce their hours and their income, but not stop working altogether, their pension can make-up the difference.

Options for retirement planning



Angela James

Pension Specialist

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Angela is a qualified Senior Financial Planner at Contractor Wealth and specialises in pension advice and financial planning for contractors.

Contractor Wealth are a specialist in offering tailored financial solutions for contractors, together with the building of excellent client relationships. [Read Full Profile...](#)

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James says there are a number of options available for contractors to consider for their retirement planning, which include:

ISAs, also known as NISAs, or New Individual Savings Accounts following the reforms of 2014, which are not as tax efficient as some alternatives but are very flexible

Pension schemes

Property, which, according to James, has been a great place to invest for contractors and generally stands the test of long-term planning

Inheritance planning.

Updated: Saturday, January 31, 2015

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