Top 10 contractor pension myths

Contractor pensions are often made out to be more complex than they need to be, and a host of myths have grown up around them.

Contractor Wealth's pensions and investments expert Angela James highlights ten of the top contractor pension myths, and explains why they are not always true.

1. I can always catch-up with my pension later - I can't afford to save for a pension now

"No you can't always catch-up," explains James. "Everyone can invest a certain amount each year tax-free, and allowances can be carried forward. But if you delay or miss out several year's contributions, the reliefs may not always be available and you have to meet certain eligibility criteria."

Any amount, no matter how small, instantly grows in value as a result of the government's tax relief on pension contributions. "Contractors early on in their careers can made modest contributions to start with, increasing them as their earnings increase," adds James.

2. I only need a pension to fund my retirement

"Contractors need to think about both the income they will need and their tax position post-retirement. What is the point of being tax efficient saving into a pension fund only to become a higher rate taxpayer (HRT) following retirement, or being penalised with a lifetime allowance charge (LTA)?

"For many contractors, it is a combination of investments, of which a pension is only one part, that may best suit their needs. Non-pension funds can also be accessed pre-retirement age, so a contractor may wish to have relatively liquid assets as well as a pension. Pensions and tax planning go hand-in-hand, and a contractor needs professional advice on both."

3. My lifestyle costs will fall when I retire

In James' experience, most contractors' lifestyles become even more expensive when they retire: "Retired contractors have so much more time on their hands, and they tend to fill it with expensive hobbies and holidays. Contractors should plan to have more disposable income on retirement, and a well-funded pension underpins this."

4. Pension funds lose money

According to James, this is a huge myth: "All investments can lose money but all investments can also make money. That's nothing to do with whether it is a pension investment, although contractors should always check the provider's fees, as if they have a small balance with lots of costs that could erode the value over the long-term.

"The key thing about any investment, pension or otherwise, is to monitor how the money is invested. It is common for contractors to take out a pension and forget all about it, assuming what was right then is right 20 years later."

5. Self-investing my pension will make it grow faster

Some contractors believe that making their own investment decisions make their funds grow faster. But the key aspect is monitoring, and a good financial adviser will be able to do this better than a contractor because the adviser has access to the tools, skills and people, as well as access to certain funds, that an individual investor won't have access to.

6. Annuities are no longer available

"Annuities are still a valid option for those contractors that need a secure income at retirement," continues James. "And not only are annuities still with us – because of the reforms of 2015, annuities are actually improving to include new features and options to stay competitive."

7. I can only buy an annuity

"This is a very outdated view – contractors have much broader options on retirement than in years past," highlights James. "This may be the only option that a contractor originally signed-up to. A financial adviser can provide information about alternatives to an annuity and how a contractor can access them."

But James warns contractors that some providers have yet to embrace the pension reforms of 2015: "Not all providers are allowing flexible access drawdown, for example."

8. Annuities are poor value

This is largely a perception rather than a fact, as James explains: "You are paying for a level of security with an annuity. If a contractor does not have significant assets on retirement and needs to secure an income, then an annuity is a valuable option for that individual.

"With an annuity, depending on the options chosen, you are paying someone else to manage your money that will continue to pay a set income, which can be index linked to increase with inflation. for as long as you live, which could be 15 years or 35 years. So, it can represent excellent value for some."

9. I can take all my pension pot as a tax-free cash lump sum

James notes that this is one of the fastest growing myths since the pension reforms of 2015: "A contractor can draw down 25% of their pension fund as a tax-free lump sum. The 2015 reforms also allow contractors to access their entire fund, assuming the scheme provider allows it, but it will be taxed at the contractor's marginal rate."

10. My family won't get my pension savings if I die

James points out that family members do benefit financially from a contractor's pension savings: "If a contractor dies before retirement, then the fund is paid to the contractor's beneficiaries as a tax-free lump sum.

"And if a contractor dies very soon after retirement, there are cases when the beneficiaries of the contractor's estate may also receive the value of the pension fund, although it would be subject to tax."


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James concludes: "Contractors can start a pension at any age and the sooner they have that conversation with a financial adviser, the better. The rules are simple: if you save well then you receive a better level of income during retirement. If you don't save well, then you can expect a poor income in retirement."

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