FINANCE UPDATES

SEPTEMBER 2021

HampshireHill Independent Financial Advisers

SELF-EMPLOYED PENSION OPTIONS

The three main types and muddied waters.

Many workers find self-employment to be a liberating change of pace from the grind of working for someone else. There are a great number of challenges involved with being your own boss, however, one of them being pensions.

In fact, many self-employed people aren't getting their retirement plan together. According to the most recent data from the Department for Work and Pensions in 2018/19, only 14% of self-employed workers paid into a pension, compared to 88% of eligible employees making payments.

Of course, the self-employed don't get automatically enrolled into defined contribution workplace pensions. They also have less incentive to start saving because there are no employer contributions into their pensions.

Pensions, however, have a hugely important role for the self-employed when it comes to retirement planning.

WHY IS A PENSION IMPORTANT?

The earlier you start saving for your retirement, the more time your pension savings have to grow. The bigger your pension pot is when the time comes to retire, the more comfortable a retirement you will have.

Consumer group Which? estimates an individual needs £19,000 a year for a comfortable retirement, while at least £13,000 is required to pay for just the bare essentials.

The new full basic state pension, in contrast, pays an individual just £9,339.20 in 2021/22, highlighting the importance of topping it up with your own pension contributions.

You build up your state pension by paying Class 2 or Class 4 National Insurance contributions, while you need 35 full qualifying years to get the new full state pension.

Generally, savers can't access their pension savings until they are aged 55 or over, so they're a great mechanism for those who might otherwise struggle to save, especially for sole traders and partners whose personal and business finances are often difficult to untangle.

Pensions can also inform your wider tax planning, with the Government offering tax relief on cash you put into your pension pot if your rate of income tax is 20%.

You can also take out 25% of your defined contribution pension as a tax-free lump sum from the age of 55.

WHAT ARE THE OPTIONS?

There are three main types of personal pensions: standard personal pensions, self-invested personal pensions (SIPPs), and stakeholder pensions.

Standard **personal pensions** allow you to choose a specific type of pension and make regular or one-off contributions.

You also pick which funds to invest in from those available from your pension provider. These funds are often managed by your provider, and invest in a range of assets in a bid to grow your savings over time.

Self-employed personal pensions (SIPP) allow investments in thousands of funds and equities. All types of funds have their own risk profiles to suit your appetite for risk.

Savers can stop and start contributions to a SIPP without any charges or penalties. You are not obliged to do anything other than what you want to do, whether that is regular payments or ad-hoc payments.

Investors can take on the responsibility for building and managing their investments within a SIPP, or they can link their SIPP to an adviser who recommends investments to choose.

These investments are then held within pension 'wrappers' until you retire, at which point they can be turned into income.

Income drawdown is a popular way to take retirement income from a SIPP, as this allows you to carry on investing after you retire while receiving an income.

Stakeholder pensions can be a low-cost pension option if you choose your provider and investments carefully.

They are somewhat of a dying breed, with only four mainstream stakeholder providers left in the UK, but can still offer value for those who only require a simple low-cost pension for which the charges are capped.

The policy terms of stakeholder pensions can be quite restrictive, meaning they have fallen out of favour among pension savers in recent years. They are also not the most flexible option for taking benefits in retirement.

This type of pension wrapper offers a relatively narrow range of funds, compared to other two options.

PENSIONS & THE ANNUAL ALLOWANCE

With any pension plan, you can put as much as you like into your pot each tax year. But before you put a penny in, you should know there is a limit on the amount that will get tax relief.

This is called the 'annual allowance', and currently stands at £40,000 for most people. A tax charge applies to any money you contribute to your pension above this allowance.

For high earners with threshold income of £200,000 or more AND adjusted income in excess of £240,000, the annual pensions allowance will be tapered.

For every £2 of adjusted income over £240,000 in 2021/22, an individual's annual allowance is reduced by £1. The minimum annual allowance is £4,000.

HOW WE CAN HELP

Hopefully, we've so far provided an insightful digest into the pension options you have so you can start to consider the options open to you.

We would still highly recommend that you talk with one of our experts about your pension, however, to ensure it's tax-efficient, wisely invested, and in line with your appetite for risk.

With more than 40,000 regulated funds on the market, each with its own risk level and investment strategy, it's not uncommon for people to have investments that don't match their needs.

According to recent studies, around half of pensions are in investments that are inappropriate for their needs and risk level.

With our help, however, you can plan with the confidence that not only is your pension being invested properly, but it is also being monitored by an expert.

Pension planning also involves deciding how you are going to unlock your savings while you're in your retirement, which we can help you do in the most tax-efficient manner.

Finally, remember, you may have other pension pots from your time in previous employment, which we can consolidate to make them easier to manage if this is the right thing to do, all the while avoiding unexpected pension charges.

Talk to us about your pension plan.

IMPORTANT INFORMATION

The way in which tax charges (or tax relief, as appropriate) are applied depends on individual circumstances and may be subject to future change. Pensions eligibility depends on individual circumstances and pension benefits cannot normally be taken until age 55.

This document is solely for information purposes and nothing in it intends to constitute advice or a recommendation. You should not make any pension decisions based on its content.

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