Pareto
ALL MATTERS FINANCIAL

A flexible, tax-efficient way of saving for your long-term future

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GUIDE TO SELF-INVESTED PERSONAL PENSION SCHEME

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Welcome to our Guide to Self-Invested Personal Pension Schemes. Saving for your retirement is one of the longest and biggest financial commitments you will ever make. Imagine you are retiring today. Have you thought about how you are going to financially support yourself, and potentially your family too, with your current pension savings?

If appropriate to your situation a Self-Invested Personal Pension (SIPP) could be an option to consider as part of your overall retirement planning. A SIPP may be appropriate for you if you're confident making your own investment decisions and managing your pension payments against the relevant allowances.

How do I know if a SIPP is right for me?

A SIPP could be right for you if you are looking for a wider choice of investment options and have sufficient knowledge and experience of investing to make your own investment decisions or have a trusted adviser to help you make these decisions.

A SIPP provides a range and flexibility of investment options that make it one of the most flexible methods of saving for retirement. You can invest money into your SIPP up until you reach age 75, and start withdrawing money from it as early as age 55 (57 from 2028).

As with all defined contribution schemes, the amount that you will have available when you retire depends on the contributions that you, and any employers, have made and how your investments perform over time.

If appropriate, almost anyone under the age of 75 in the UK could open and make tax-relievable contributions into a SIPP. Parents can even open a Junior SIPP for their children. SIPPs are not suitable for every investor and other types of pensions may be more appropriate.

As with all pensions, SIPPs provide favourable tax treatment. Once in a SIPP wrapper, your savings will grow free from UK income tax and capital gains tax.

Do the same tax and contribution rules apply to a SIPP as other pensions?

A SIPP enables you to save and grow your money so that you can see your retirement dreams come to life. They are governed by the same tax and contribution rules as other pensions. Anyone living in the UK who pays into a SIPP is eligible to claim pension tax relief, including low-income earners.

Tax relief is paid on your pension contributions at up to the highest rate of income tax you pay. Basic rate and non-taxpayers receive 20% pension tax relief. Higher rate taxpayers can claim 40% pension tax relief and additional rate taxpayers can claim 45% pension tax relief on any contributions matched by income taxable at those rates.

In Scotland, income tax is banded differently, and pension tax relief is applied in a slightly different way. Starter rate taxpayers pay 19% income tax but get 20% pension tax relief. Basic rate taxpayers pay 20% income tax and get 20% pension tax relief. Intermediate rate taxpayers pay 21% income tax and can claim 21% pension tax relief. Higher rate taxpayers pay 41% income tax and can claim 41% pension tax relief. Top rate taxpayers pay 46% income tax and can claim 46% pension tax relief.

A Lifetime Allowance applies to the total of all the pensions you have, including the value of pensions promised through any defined benefit schemes you belong to, but excluding your State Pension.

The Lifetime Allowance for the tax year 2021/22 is £1,073,100. When you wish to withdraw your retirement funds, or on death before 75 or at age 75 if you have not drawn benefits, if the total value exceeds this limit then you will be liable to a tax charge on the amount above the Lifetime Allowance limit.

Is tax relief on a SIPP subject to the Annual Allowance?

You may contribute up to the value of your earned income to a pension in any tax year (or £3,600 if more) and receive income tax relief on those contributions. Your employer can make contributions on your behalf and receive corporation tax relief as long as those contributions are deemed to be made wholly and exclusively for the purposes of the business (tax-relievable employer contributions aren't limited by your earnings).

Then in addition to the tax relief rules above, all contributions combined (your own, your employer's and any third party contributions) are subject to the Annual Allowance, which is currently £40,000 for the tax year 2021/22. If your total income is over £200,000 you may have a reduced Annual Allowance.

YOU CAN NORMALLY TAKE MONEY FROM YOUR SIPP WHEN YOU REACH AGE 55 (INCREASING TO 57 FROM 2028). WHEN AND HOW YOU TAKE YOUR MONEY CAN MAKE A BIG DIFFERENCE TO HOW MUCH TAX YOU MIGHT PAY AND HOW LONG YOUR MONEY WILL LAST

The Annual Allowance is a gross figure, meaning that when calculating how much you may add to your pension, you could consider your own personal contributions, your employer's contributions, any other contributions and tax relief. If you exceed the Annual Allowance you may have to pay a tax charge.

If you earn more than the Annual Allowance or are looking at employer contributions, and you have not contributed up to the full allowance in the previous three tax years, you may be able to make a larger contribution in the current tax year, using 'carry forward'.

This enables you to make use of any unused portion of the Annual Allowance from the previous three years as long as you had a pension plan in existence in those earlier years. Regardless of the amount of unused allowance you may have available, you may not personally contribute more to a pension than you have earned in the current tax year (or £3,600 if more).

Should I consider consolidating my pensions into one SIPP plan?

During your working life you may have built up pension pots with several employers. This can often make it hard to keep track of them all and manage them well. For simplicity, it may make sense to consolidate your pensions into one plan.

Modern flexible pension plans offer benefits that older plans do not, for example, flexi-access drawdown of your pension, or access to an income for your loved ones on your death.

Having several pension plans may mean you have more paperwork to keep track of. You may also have a range of different investments that you will need to review and make decisions about.

If you have a few pension plans, including some older ones that you may not have checked for some time, it is a good idea to review the charges. Higher charges can eat away at any investment returns.

There is no guarantee you will be better off as a result of transferring and we advise you take professional financial advice before you move a pension plan, to make sure you understand all the implications.

TIME TO GET BACK TO DREAMING ABOUT YOUR RETIREMENT, NOT DREADING IT?

MAKING THE RIGHT CHOICE NOW COULD MAKE A BIG DIFFERENCE TO HOW MUCH MONEY YOU HAVE IN THE FUTURE, AND SAVING INTO A PENSION PLAN COULD HELP YOU ACHIEVE THE LIFESTYLE YOU WOULD LIKE. YOU'RE NEVER TOO YOUNG TO SAVE FOR RETIREMENT.

What flexibiliry at retirement do I have to take money from my SIPP?

You normally take money from your SIPP when you reach age 55 (increasing to 57 from 2028 unless you already have a plan with a protected pension age)). When and how you take your money can make a big difference to how much tax you might pay and how long your money will last.

There are different ways you can take money from your SIPP. Keep in mind that you can choose one option or a combination of options.

Annuities - Guarenteed income for life or for a specific period

Annuities enable you to exchange your SIPP fund for a guaranteed income for life or a specific period. They were once the most common pension option to fund retirement.

You can normally withdraw up to 25% of your SIPP as a one-off tax-free lump sum, then convert the rest into a taxable income for life via an annuity. There are different lifetime annuity options and features to choose from that affect how much income you may receive. You can also choose to provide an income for life for a dependent or other beneficiary after you die.

The amount you receive depends on how long the provider expects you to live, how many years they'll have to pay you and any additional benefits you have, such as a guaranteed payment period or index linking.

Flexible retirement income - Flexi-access drawdown

When it comes to assessing your options, flexibility is the main attraction offered by flexi-access drawdown plans, which allow you to access your money while leaving it invested, meaning your funds can continue to grow.

This option normally means you take up to 25% of your SIPP as a tax-free lump sum or a series of smaller lump sums. The remaining funds stay invested to provide you with a taxable income.

You may draw your income as a regular amount or simply draw funds as and when you need. Your unlike a lifetime annuity, your income isn't guaranteed for life.

Small cash sum withdrawals - Uncrystallised funds person lump sums (UFPLS)

If you decide not to draw your tax free lump sum as a one-off sum, you may opt to take your income as a single lump sum or series of Uncrystallised Funds Pension Lump Sums without placing your funds in flexi-access drawdown. Each time you withdraw an amount from the SIPP as an UFPLS, the first 25% taken is tax-free, whilst the remaining 75% is taxable income. The rest of your SIPP remains invested until you need to withdraw more cash.

Combination - Mix and match

It may suit you better to use a combination of the options outlined above. For example, you might want to use some of your savings to purchase an annuity to cover the essentials, for example, rent, mortgage or household bills, with the rest placed in flexi-access drawdown so that you may decide how much you wish, and can afford, to withdraw and when.

Alternatively, you might want more flexibility in the early years of retirement and more security in the later years. If that is the case, this may be a good reason to delay purchasing an annuity until later in life.

Can I use my SIPP as partial security against a loan to borrow money?

SIPP lending or borrowing is when your SIPP is used as partial security against a loan to borrow more money and increase its investment capacity. There are numerous rules around SIPP lending and we recommend you should take professional financial advice if you are considering this option.

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The document is based upon our understanding of current rules and legislation. Personal circumstances differ and not all of this information is applicable to every client and/or their business, this information is general in nature and should not be relied upon without seeking specific professional financial advice.

You cannot normally access your pension until age 55 (this will rise to age 57 in April 2028).

Tax treatment depends on individual circumstances and all tax rules may change in the future.

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