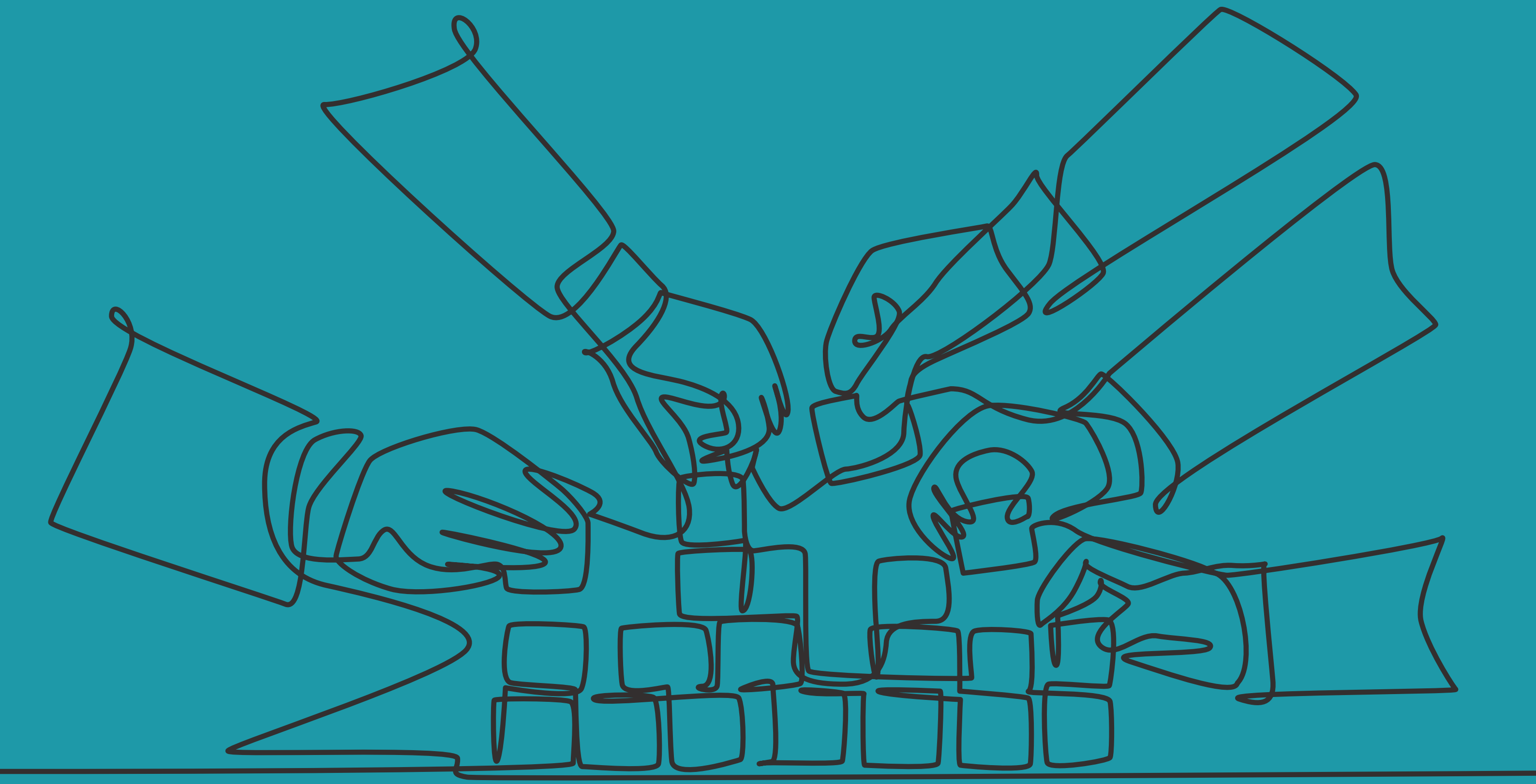
The complete guide to pension contributions

How much you should pay in, when to start, and how to maximise your tax relief



KILLIK & Co

Pension contributions

Building wealth for retirement is one of the most important financial journeys you will undertake in your lifetime.

Whether you are employed, self-employed, or running your own business, understanding how much and when to contribute to your pension can make the difference between a comfortable retirement and financial uncertainty.

If you have ever wondered whether you are contributing enough to your pension, how to make the most of tax relief, or how to balance pension saving with other financial priorities, you are not alone. Many people find pension contribution rules complex and struggle to determine the optimal strategy for their circumstances.

This is why we have created this complete guide to pension contributions.

Pension contributions are not just about meeting minimum requirements or following generic advice. They are about creating a personalised plan that aligns with your income, lifestyle, career, and retirement aspirations.

The following pages will reveal everything you need to know about pension contributions, from the basics of *annual allowances* and tax relief to strategies for maximising your retirement savings. We will explore how employed and self-employed individuals can optimise their contributions, the importance of starting early, and how professional advice can help you navigate the complexities of pension planning.

What are pension contributions, and why do they matter?

Pension contributions are the payments you make into your pension scheme to build savings for retirement.

These contributions can benefit from government tax relief and, for employed individuals, are often supplemented by employer contributions that can further boost your retirement pot.

The main purpose of pension contributions is to accumulate sufficient wealth to maintain your desired lifestyle when you stop working. Unlike other forms of saving, pension contributions receive preferential tax treatment, making them one of the most tax-efficient ways to build long-term wealth.

You can make contributions to several types of pension schemes, including:

- Workplace pensions through your employer
- Personal pensions that you arrange independently
- *Self-Invested Personal Pensions (SIPPs)* for greater investment control
- Stakeholder pensions with capped charges and flexible contributions

However, it is crucial to understand that pension contributions are subject to *annual limits and specific rules* depending on your employment status, income level, and the type of pension scheme you choose. The timing and amount of your contributions can have a significant impact on your final retirement income through the power of compound growth and tax relief.

How do pension contribution rules work?

The framework for pension contributions involves several key rules and limits that determine how much you can pay in and when you can access your savings.

Understanding these rules is essential for maximising your retirement planning strategy.

Annual allowance

For the 2025/26 tax year, you can contribute up to £60,000 or 100% of your UK relevant earnings (whichever is lower) across all your pension schemes. This annual allowance includes your personal contributions, any employer contributions, and triggers tax relief added by the government.

Earnings requirement

You need UK-relevant earnings to make personal contributions and receive tax relief. However, even those with no earnings can contribute up to £3,600 gross (£2,880 net) annually to a pension.

High earners with adjusted income over £260,000 face a reduced annual allowance. For every £2 above this threshold, the allowance reduces by £1, down to a minimum of £10,000 for the 2025/26 tax year.

The process for making contributions varies depending on whether you are employed or self-employed:

For employed individuals

Contributions can be made through *salary sacrifice, net pay arrangements, or relief at source*, with employers often matching or supplementing your contributions.

For self-employed individuals

You make personal contributions to your chosen pension scheme and claim tax relief through Self-Assessment if you are a higher or additional rate taxpayer.

For company directors

You can make both personal contributions and employer contributions (through your limited company), providing additional tax efficiency opportunities.

Carry forward

If you have not used your full annual allowance in previous tax years, you can carry forward unused allowances from the last three tax years, provided you were a member of a pension scheme in those years.

Understanding tax relief on pension contributions

Understanding how tax relief on your pension savings works can help you maximise the value of your contributions and build wealth more effectively.

20%

Basic rate tax relief

All pension contributions automatically receive basic rate tax relief. This means a £100 contribution to your pension only costs you £80 from your take-home pay, with the government adding the remaining £20.

40%

Higher rate tax relief

If you pay Income Tax at 40%, you can claim additional tax relief through your Self-Assessment tax return. This brings your total tax relief to 40%, making a £100 pension contribution cost just £60 from your take-home pay.

45%

Additional rate tax relief

Additional rate taxpayers can claim even more tax relief, making a £100 contribution cost only £55 from their take-home pay.

Salary sacrifice

With salary sacrifice arrangements, you do not need to claim tax relief separately. Your employer reduces your salary before calculating tax and National Insurance contributions, so you automatically receive full tax relief at your marginal rate. This means higher and additional rate taxpayers receive their full 40% or 45% tax relief immediately, without needing to claim it back through Self-Assessment.

Corporation tax relief

For company directors making employer contributions through their limited company, these contributions can be deductible against Corporation Tax at 19% or 25%, depending on the company's profit level, rules and tests.

How tax relief is applied

The method of applying tax relief depends on how you make your contributions:

Relief at source

Most personal pension schemes use this method. You pay the net amount (after basic rate tax relief), and your pension provider claims the basic rate relief from HMRC. Higher and additional rate taxpayers then claim extra relief through Self-Assessment.

Net pay arrangements

Common in workplace schemes, your pension contributions are deducted from your gross pay before tax is calculated, giving immediate tax relief at your marginal rate.

Salary sacrifice

Your employer reduces your salary by the contribution amount and pays this into your pension instead. This saves both Income Tax and National Insurance contributions, making it highly tax-efficient.

Employed vs self-employed pension contributions?

The approach to pension contributions varies significantly depending on your employment status. Understanding these differences is crucial for optimising your retirement savings strategy.

If you are employed

All eligible employees are now automatically enrolled into their workplace pension scheme with minimum total contributions of 8% (5% employee, 3% employer) of qualifying earnings. The most important rule for employed individuals is to maximise employer contributions. This is essentially free money that can double or triple your effective contribution rate.

Beyond employer matching, you can contribute more to your workplace scheme or set up a SIPP for greater investment flexibility.

Many employers offer salary sacrifice arrangements that save both Income Tax and National Insurance contributions, typically saving an additional 12% for basic rate taxpayers.

If you are self-employed

As a sole trader, you cannot receive employer contributions as you have no employer, making personal contributions even more important for building retirement wealth.

In this case, you can contribute when your income allows rather than through fixed monthly deductions, which is valuable for those with irregular or seasonal earnings.

If you are a company director and operate through a limited company, your business can make employer contributions on your behalf, creating additional tax efficiency opportunities.

You can potentially contribute larger percentages of your income compared to employed individuals, subject to the annual allowance.

Tax treatment depends on individual circumstances and may change in future.

Practical contribution examples

Employed individual earning £40,000

Minimum auto-enrolment: £3,200 total (£2,000 employee + £1,200 employer)

Recommended 15% target: £6,000 total (£4,800 employee + £1,200 employer)

Net cost to employee: £3,840 from take-home pay (after 20% tax relief on the £4,800 employee contribution). Subject to the financial situation of the business.

Self-employed individual earning £40,000

No employer contributions available

15% target: £6,000 personal contribution

Net cost after tax relief: £4,800 from take-home pay (a cost of £1,200 more than employed equivalent)

Company director earning £40,000

Combined approach: £3,000 employer contribution + £3,000 personal contribution

Total: £6,000 (15% of earnings)

Net cost to individual: £2,400 from take-home pay (after 20% tax relief on £3,000 personal contribution). The individual claims personal tax relief on personal contribution

Additional company saving: Corporation Tax relief on £3,000 employer contribution

Out of the three examples above, the company director pays the least out of their personal take-home pay.

When should you start contributing, and how much is enough?

The timing and amount of your pension contributions can dramatically impact your final retirement income. Starting early and contributing consistently are two of the most powerful strategies for building retirement wealth.

Starting early

Due to *compound growth*, small contributions made early in your career can outperform much larger contributions made later. A 25-year-old contributing £200 per month could accumulate more wealth by retirement age than a 40-year-old contributing £500 per month.

Contribution guidelines

It is typically recommended to contribute around 8% of your gross income throughout your working life, in addition to any employer contributions, which are usually around 3%. This provides a solid foundation for maintaining your lifestyle in retirement.

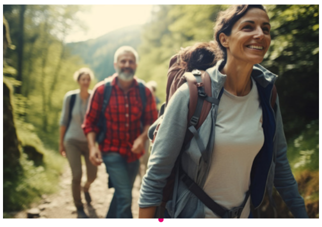
Age-based approaches

Some Advisers suggest contributing half your age as a percentage of your salary. Under this approach, a 30-year-old would contribute 15%, while a 50-year-old would contribute 25%.

Contribution strategies by life stage

Starting your career (20s-30s)

If you're just *starting your career*, you'll want to focus on establishing consistent contribution habits. You can do this by maximising employer contributions, even if other contributions are minimal. Plus, take advantage of compound growth over long periods of time. Small investments when you're starting your career could have more impact than larger investments made later. You might also want to consider higher-risk investments for potentially greater returns.



Mid-career (30s-50s)

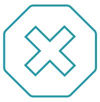
If you're in the middle of your career, you can look to increase contributions as your income grows. This includes making catch-up contributions if you started late. You'll also need to balance pension contributions with other priorities like mortgages and family expenses, so reviewing and optimising investment strategies regularly will be key.

Pre-retirement (50s-65)

As you get closer to retirement, you'll want to start maximising your contributions. You can do this by considering carry-forward opportunities for unused allowances and planning tax-efficient withdrawal strategies. Ensure you review risk levels and adjust your portfolios accordingly.

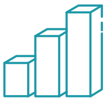
Balancing pension contributions with other financial priorities

While pension contributions are important, they should fit within your broader financial strategy. For example, consider:



Emergency funds

Ensure you have 3-6 months of expenses saved in accessible accounts before maximising pension contributions.



High-interest debt

Pay off credit cards and personal loans before increasing pension contributions beyond employer matching, as the guaranteed saving typically exceeds investment returns.

Property goals

Balance pension saving with house deposit requirements, using ISAs for shorter-term accessibility while maintaining steady pension contributions for *long-term wealth building*.

Family financial security

Consider life insurance and family protection alongside pension planning to ensure comprehensive financial security.

Financial freedom

Find a sustainable contribution level that allows you to enjoy life today while securing your future, avoiding over-saving that compromises current wellbeing.

Maximising your annual allowance and using carry forward

Understanding and optimising your use of pension allowances can significantly boost your retirement savings, particularly if you have a variable income or started contributing later in your career.

Annual allowance optimisation

The £60,000 annual allowance applies to total contributions from all sources. This includes employer contributions for employed individuals, which means personal contribution capacity may be lower than expected.

Carry forward rules

You can use unused annual allowances from the previous three tax years to make larger contributions, provided you:

- ✓ Were a member of a pension scheme in each year you carry forward from
- ✓ Have used your current year's full allowance first
- ✓ Have sufficient earnings to support the total contribution

Carry forward can be particularly valuable for:

- Self-employed individuals with variable income who can contribute more during good years
- Those receiving bonuses, inheritance, or property sale proceeds
- People who started pension planning late and want to catch up
- Business owners who can time contributions to optimise tax efficiency

Carry forward examples

Example 1

Self-employed consultant Sarah is a freelance consultant who has earned £30,000, £40,000, and £50,000 in the last three years, contributing £3,000, £5,000, and £6,000 respectively. This year she earns £80,000 and wants to make a large contribution.

Her carry-forward capacity:

Year 1: £30,000 - £3,000 = £27,000 unused
Year 2: £40,000 - £5,000 = £35,000 unused
Year 3: £50,000 - £6,000 = £44,000 unused

Current year: £60,000 available

Total contribution capacity: £166,000 (subject to 100% earnings limit of £80,000). Maximum contribution this year: £80,000 (gross figure, including 20% tax relief).

Example 2

Company Director James runs a limited company and makes minimal pension contributions. He wants to make a large contribution before retirement using accumulated profits.

Previous three years' unused allowances: £45,000, £50,000, £55,000
Current year allowance: £60,000

Total capacity: £210,000

His company can make employer contributions up to this limit (subject to his earnings and the company having sufficient profits), providing significant Corporation Tax relief.

Money purchase annual allowance: what you need to know

Once you start taking flexible benefits from your pension, your future contribution capacity becomes significantly restricted through the Money Purchase Annual Allowance (MPAA). Understanding this rule is crucial for planning your retirement income strategy.

MPAA triggers

The £10,000 MPAA applies if you:

- Take income drawdown from your pension via *flexi-access*
- Take uncrystallised fund pension lump sums (UFPLS)
- Take cash from a flexible access drawdown fund

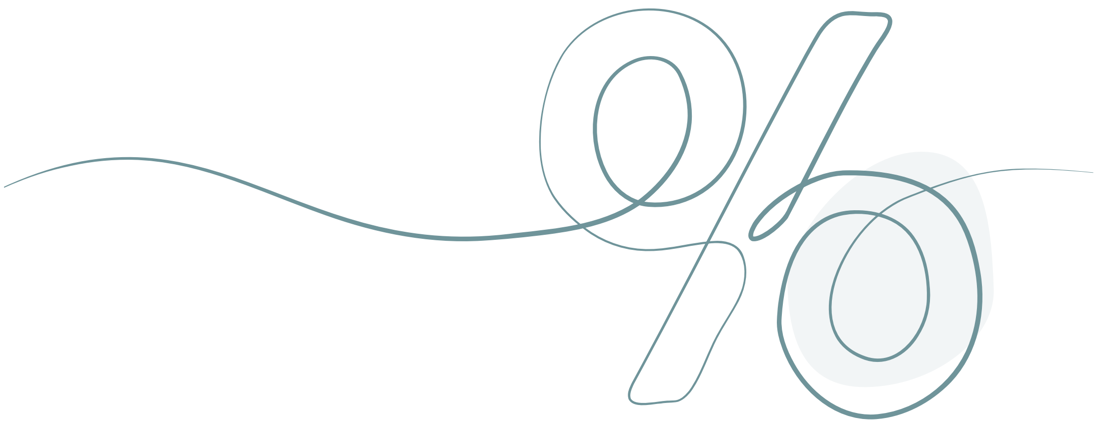
MPAA restrictions

Once triggered, you can only contribute £10,000 annually to money purchase pensions (including SIPPs), and you cannot use carry forward to increase this amount.

Planning implications

The MPAA significantly impacts your ability to continue building pension wealth after retirement, making it important to:

- Maximise contributions before triggering the MPAA
- Consider delaying flexible access if you want to continue contributing
- Plan alternative savings strategies for post-retirement wealth building



Avoiding unnecessary MPAA triggers

Pension commencement lump sum

Taking your 25% tax-free cash as a pension commencement lump sum (while leaving the remaining 75% invested without drawing income) does not trigger the MPAA.

Lifetime annuities

Purchasing a traditional lifetime annuity does not trigger the MPAA, allowing continued contributions to other pensions.

Defined benefit pensions

Drawing benefits from defined benefit (final salary) pension schemes does not trigger the MPAA.

Capped drawdown

If you have existing capped drawdown arrangements, taking income from these does not trigger the MPAA.

Planned approach

Structure your retirement income to avoid triggering the MPAA until you are certain you no longer need high contribution capacity.

Self-employed pension contributions – what you need to consider

Self-employed individuals face unique challenges and opportunities when it comes to pension contributions.

Without the safety net of employer contributions and auto-enrolment, *self-employed pension planning* requires greater discipline and strategic thinking.

Contribution capacity

Self-employed individuals can contribute up to 100% of their net relevant earnings (profits after business expenses) or £60,000, whichever is lower. This often allows for higher percentage contributions than employed individuals.

Tax relief claims

Basic rate tax relief is applied automatically, but higher and additional rate taxpayers must claim extra relief through their Self-Assessment tax return.

Irregular income management

Self-employed individuals with variable incomes can benefit from flexible contribution timing and carry forward rules to optimise pension savings.

Company Directors: dual contribution strategies

Company directors who pay themselves through a combination of salary and dividends have unique opportunities for tax-efficient pension contributions:

Personal contributions

Made from salary or relevant earnings, attracting personal tax relief at the individual's marginal rate.

Employer contributions

Made directly by the limited company, deductible against Corporation Tax and not treated as a benefit-in-kind for the director.

Many directors use a combination approach, taking a small salary (typically around the National Insurance threshold) and making large employer pension contributions to minimise both personal tax and National Insurance while maximising Corporation Tax relief.

Self-employed contribution examples

Sole Trader earning £50,000 profit

Maximum contribution: £50,000 (100% of earnings)

15% target: £7,500 annual contribution

After 20% tax relief: £6,000 from take-home pay

Higher-rate taxpayer: Additional £1,500 relief through Self-Assessment

Company Director with £100,000 company profits

Strategy: £12,570 salary + £25,000 employer pension contribution

Remaining profits: £62,430 available as dividends

Tax savings: Significant reduction in Corporation Tax, Income Tax, and National Insurance

Personal contribution options: Additional contributions from dividend income

Optimising pension contributions for high earners

High-earning individuals face additional complexities in pension planning, including tapered annual allowances, higher tax rates, and more sophisticated tax planning opportunities.

Tapered annual allowance

Individuals with adjusted income over £260,000 face a reduced annual allowance, calculated as:

- **Standard allowance:** £60,000
- **Reduction:** £1 for every £2 of income above £260,000
- **Minimum allowance**: £10,000 (at £360,000+ income)

Threshold income test

The tapering only applies if threshold income (broadly, income minus pension contributions) exceeds £200,000. Strategic pension contributions can sometimes keep individuals below this threshold.

High-earner strategies

- Salary sacrifice to reduce adjusted income and avoid tapering
- Timing of bonus payments and pension contributions
- Use of carry forward before tapering takes effect
- Alternative savings strategies when pension allowances are restricted, such as *stocks and shares ISAs*

Family pension planning – contributing for loved ones

Pension contributions are not limited to your own retirement planning. Understanding how to contribute for family members can create additional tax-efficient wealth building opportunities.

Spousal contributions

You can contribute to your spouse's pension even if they have no earnings, up to £3,600 gross annually. Gifts between spouses have no tax implications due to the spousal exemption. This can be valuable for:

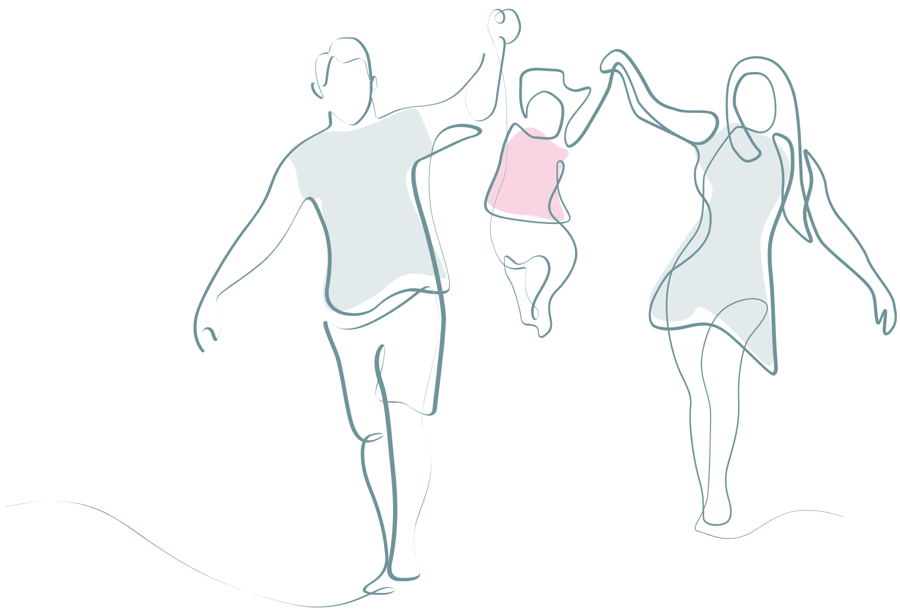
- Non-working spouses or those with low incomes
- Optimising household tax efficiency
- Building retirement security for both partners

Junior SIPPs

You can contribute up to £3,600 annually to a pension for your children or grandchildren, providing them with a substantial head start for retirement through decades of compound growth.

Family tax planning

Strategic use of family pension contributions can help manage household tax liabilities while building long-term wealth for the entire family.



Junior SIPP benefits

Thanks to compound growth, a £3,600 annual contribution to a Junior SIPP for a child could potentially grow to hundreds of thousands of pounds by their retirement.

£3,600 contributed annually from birth to age 18, then left to grow

Total contributions: £64,800

Potential value at age 65 (assuming 5% annual growth*): Over £800,000

Impact: Financial security and independence for the next generation

**5% growth figure shown is for illustrative purposes only. It is not a reliable indicator of future performance, which may be volatile and inconsistent. As with all investments, the value can fall as well as rise, and you may not get back the amount you originally invest.*

When and why to seek professional advice

While basic pension contribution planning can be straightforward, the rules become increasingly complex as your income rises, your circumstances change, or you approach retirement.

Professional advice can help you navigate these complexities and optimise your wealth planning.

When to seek advice

- Annual income over £100,000, where tax planning becomes more complex and beneficial
- Self-employed individuals with variable income or multiple business interests
- Approaching retirement and planning withdrawal strategies
- Significant life changes such as career changes, inheritance, or family circumstances
- Multiple pension schemes requiring coordination and optimisation

The value of professional advice:

- Personalised contribution strategies based on your specific circumstances
- Tax-efficient planning that considers all aspects of your financial situation
- Investment management and portfolio construction
- Regular reviews and adjustments as your life evolves
- Peace of mind that your retirement planning is on track

Killik & Co's approach to pension contribution planning

At Killik & Co, our Wealth Planners work with you to create comprehensive pension contribution strategies that integrate with your broader financial planning. Our approach includes:

Holistic assessment

We consider your entire financial situation, not just pension contributions, to ensure optimal outcomes across all areas of your wealth.

Personalised strategies

You'll receive a tailored contribution plan based on your income, career stage, retirement goals, and family circumstances.

Tax optimisation

We help clients maximise tax relief and minimise tax liabilities through strategic contribution planning and timing.

Investment management

Our award-winning* SIPP provides access to our full investment universe with professional portfolio management. (Tax treatment depends on individual circumstances and may change in future).

Ongoing support

Regular reviews ensure your contribution strategy remains optimal as your circumstances and the tax thresholds evolve.

**Past performance is not an indicator of future results.*

Start optimising your pension contributions today

As explored throughout this guide, pension contributions are one of the most powerful tools available for building long-term wealth and securing your financial future.

The combination of tax relief, potential employer contributions, and compound growth over time makes pension saving a crucial investment.

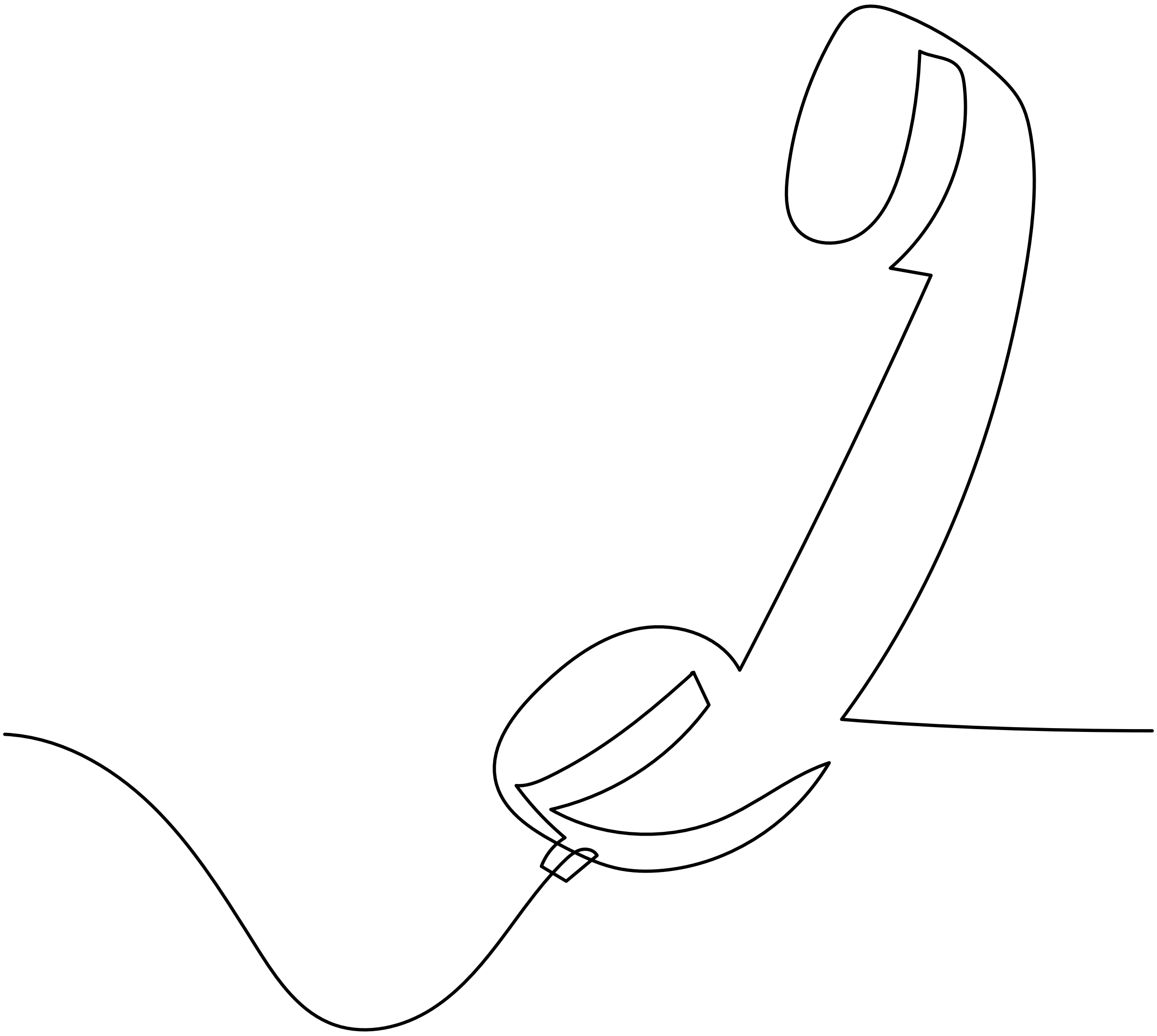
However, optimising your pension contribution plan requires more than simply following generic rules or contributing the minimum amounts. It requires understanding your personal circumstances, career trajectory, and retirement aspirations, then crafting a strategy that evolves with your life.

The key principles to remember are:

- **Start early** | Time is your greatest asset in pension planning. Even small contributions made early can outperform larger contributions made later.
- **Maximise tax relief** | Take full advantage of the generous tax relief available on pension contributions, particularly if you are a higher or additional rate taxpayer.
- **Use all available allowances** | Understand and optimise your use of annual allowances and carry forward opportunities.
- **Consider your employment status** | Employed and self-employed individuals have different opportunities and challenges that require tailored approaches.
- **Plan holistically** | Balance pension contributions with other financial priorities and life goals.
- **Review regularly** | Your contribution strategy should evolve as your income, circumstances, and goals change.
- **Seek professional guidance** | Complex rules and regulations mean professional advice can add significant value, particularly for higher earners or those with complicated circumstances.

Whether you are just starting your career or approaching retirement, the decisions you make about pension contributions today will significantly impact your financial security tomorrow. By developing your understanding, maximising opportunities, and seeking appropriate guidance, you can build the retirement you truly want.

If you are ready to optimise your pension contribution strategy, *speak to a Killik & Co Adviser today* to explore how we can help you build wealth effectively for the retirement you deserve.



020 7337 0777

info@killik.com

www.killik.com

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