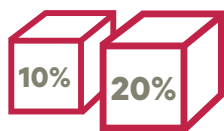


# Reducing CGT on gains using pension contributions

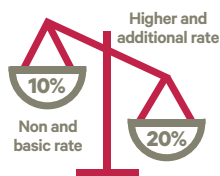
## Tech-Bites

A look at how making pension contributions can reduce the rate of capital gains tax payable on all or part of a taxable gain.

### Key Points



There are two rates of capital gains tax\* (CGT).



For non and basic rate taxpayers the rate is 10%\* and for higher and additional rate taxpayers the rate is 20%\*.

### INCOME TAX + TAXABLE GAIN

Any taxable gain is added to an individual's total income. Any part sitting within the basic rate band is taxed at 10%\* and any part in the higher or additional rate bands is taxed at 20%\*.



Pension contributions can be used to reduce total income so that all or part of any gain falls into the basic rate of tax, thereby reducing the level of CGT payable on the gain.

\* Except gains on disposal of residential property not qualifying for private residential relief and carried interest – 18% and 28% rates still apply

### How are capital gains taxed?

There are two rates of CGT\*:

- 10%\* for non and basic rate taxpayers
- 20%\* for higher and additional rate taxpayers

There is an annual exemption of £12,300 (2020/21), within which any gains are free from CGT. The taxable gain is added to an individual's total income, where:

- Any gains falling into the non and basic rate bands are subject to the 10%\* CGT rate; and
- Any gains falling into the higher or additional rate bands are subject to the 20%\* CGT rate

\* Except gains on disposal of residential property not qualifying for private residential relief and carried interest – 18% and 28% rates still apply

### CGT TAX RATES

Non taxpayers: Basic rate taxpayers

**10%\***

Higher rate taxpayers: Additional rate taxpayers

**20%\***

## How can making a personal pension contribution reduce CGT?

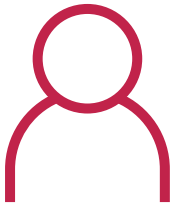
### A personal pension contribution can:

- Reduce the level of income subject to higher and/or additional rates
- Build retirement benefits

### It can also result in reducing CGT by:

- Bringing all or part of the taxable gain into the basic rate band
- Reducing the rate of CGT payable on all or part of the taxable gain
- The personal pension contribution must be made in the same tax year in which the capital gain is realised.

### Example - Bill



- Has earned income of £50,000.
- Has a taxable gain of £5,000 in excess of the annual exemption.
- The CGT payable will all be at the 20% rate as it sits within the higher rate when added to his income.

### If Bill makes a net pension contribution of £4,000

- This will be grossed up to £5,000 in his pension
- It will also extend his basic rate band by £5,000
- Therefore all his income and the taxable gain falls within the basic rate band
- Now Bill only pays 10% CGT on the gain

#### Before realising the taxable gain

£12,500 Personal allowance

£37,500 Basic rate

#### After realising the taxable gain

£12,500 Personal allowance

£37,500 Basic rate

£5,000 TAXABLE GAIN Higher rate

CGT at 20%

#### After a grossed-up pension contribution of £5,000 is made, the realised gain falls into the basic rate tax band

£12,500 Personal allowance

£37,500 + £5,000 TAXABLE GAIN Basic rate

CGT at 10%

### By making the pension contribution, Bill has:

- Built further retirement benefits
- Reduced the rate of CGT due on his taxable gain

### Effective tax saving and relief in pension contribution:

£500 in CGT

£1,000 in tax relief in pension

30% = effective rate of tax relief

## Planning considerations

### MAXIMISING PENSION BENEFITS



#### Making pension contributions can help clients:

- Build up retirement benefits
- Utilise any carry forward of unused allowance

### MITIGATING TAX



#### Pension tax planning can help clients:

- Reduce a CGT bill on a taxable capital gain
- Reduce tax payable on other gains
- Reclaim all or part of personal allowance
- Eliminate all or part of the high income child benefit tax charge

This document is based on Canada Life's understanding of applicable UK tax legislation and current HM Revenue & Custom's practice, as at March 2020 and could be subject to change in the future. It is provided for professional advisers only. Any recommendations are the adviser's sole responsibility.



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