

Reclaiming the Personal Allowance

Tech-Bites

A look at how making a pension contribution can help individuals reclaim all or part of their personal allowance where this has been lost.

Key Points



Individuals with adjusted net incomes in excess of £100,000, lose their personal allowance at a rate of £1 for every £2 of income over £100,000.



In the tax year 2020/2021, for adjusted net incomes over £125,000, an individual's personal allowance is completely lost.

£12,500

Making a pension contribution, where it reduces adjusted net income below £125,000, can potentially allow an individual to reclaim part or all of their personal allowance.



The effective rate of tax relief on the personal pension contribution can be as much as 60%.

Reclaiming all or part of the personal allowance

How is the personal allowance lost?

The personal allowance is reduced as follows:

- For every £2 of adjusted net income over £100,000, an individual loses £1 of their personal allowance
- In the 2020/21 tax year, this results in the complete loss of the personal allowance for adjusted net incomes over £125,000

How can making a pension contribution help?

Making a pension contribution can:

- Effectively reduce an individual's adjusted net income
- Reduce income to under £125,000 enabling them to reclaim part of their personal allowance
- Enable individuals to reclaim the full personal allowance where adjusted net income is reduced to £100,000 or less

Standard tax bands (2020/21 tax year)

Personal allowance	Basic rate tax band	Higher rate tax band	Additional rate tax band	
£12,500*	Next £37,500**	Next £112,500**	Over £150,000**	
Tax Rate	0%	20%	40%	45%

Tax bands for adjusted net incomes over £125,000

Personal allowance	Extended basic rate tax band	Higher rate tax band	Additional rate tax band
£0	First £37,500**	Next £112,500**	Over £150,000**
Tax Rate	20%	40%	45%

Adjusted net income reducing from £125,000 to £100,000 due to pension contribution

Personal allowance	Extended basic rate tax band	Higher rate tax band	Additional rate tax band	
£12,500*	Next £37,500** + £25,000	Next £112,500**	Over £175,000**	
Tax Rate	0%	20%	40%	45%

* The personal allowance is reduced to zero at a rate of £1 for every £2 over £100,000
 ** Different rates and bands apply in Scotland

Example - Sandra



- Sandra has adjusted net income of £125,000; and
- Has therefore lost her personal allowance

Can making a pension contribution help Sandra reclaim her lost personal allowance?

If Sandra makes a net pension contribution of £20,000, she can:

- Benefit from a grossed up pension contribution of £25,000
- Receive higher rate tax relief (through a self assessment tax return)
- Reduce her adjusted net income down to £100,000
- Reclaim her full personal allowance of £12,500

If Sandra makes a net pension contribution of £20,000 into her pension:

£20,000 (grossed up to £25,000)	→	Basic rate relief in pension	£5,000
Higher rate relief available on gross contribution	→	Higher rate relief in pension (via tax return)	£5,000
Higher rate relief available on gross contribution	→	Tax saving on reclaiming personal allowance	£5,000
		Effectively tax saving and relief in pension	£15,000

Effective cost to Sandra:

£10,000

Effective rate if tax relief is:

60%

Planning considerations

Maximising pension benefits

Pension tax planning can help clients:

- Make full use of the annual allowance
- Utilise any carry forward of unused allowances
- Build up retirement benefits

Mitigating tax

Pension tax planning can help clients:

- Reclaim part or all of the personal allowance (up to £12,500 for 2020/21)
- Effectively get up to 60% tax relief on a pension contribution
- Reduce their overall levels of income tax
- Reduce tax due on other investment income or gains within the tax year

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.



Pension Contributions & Tax Relief | Technical Services: www.canadalife.co.uk/ican

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