



# Tax and your pension

## Video transcript

Hello and welcome to this webinar about tax and your pension. My name is Rebecca Dodd and I'm a pensions consultant from Mercer. The aim of the webinar is to give you a better understanding of how tax relief is applied to pension savings and when benefits might be subject to income tax. But first of all, today we'll have a look at your benefits in USS so how it all works.

Then we'll move on to tax relief on your contributions and then paying tax on your benefits once in retirement. Then we'll finish off with a look at the calculators and tools that can help you understand your pension, so the options available to your retirement and any tax implications that you could face.

Let's take a look at how your benefits and savings in USS can build up. There's two main types of pension in the UK, the defined benefit (DB) and defined contribution (DC), and USS has got both these types of benefits. Defined benefit (DB) means that your benefits on retirement are based on a predetermined formula. In USS, the pension that you build up depends on the salary that you earn each year up to a certain threshold, the years that you've been working and a pension build-up rate. The pension that you build up is not directly connected to how much you or your employer's paid in; what matters is your formula. The defined benefit (DB) part of USS is called the Retirement Income Builder.

There's also a defined contribution (DC) part of USS which is called the Investment Builder. In a defined contribution (DC) arrangement, any money paid in by you or your employer goes into your pot. Then at retirement, your benefit is based on the value of your pot of money so it's completely dependent on how much has been paid into your pot and how it's grown over the years. In general, you tend to have more flexibility in how and when you can take defined contribution (DC) savings.

In the defined contribution (DC) part, the Investment Builder, you can choose where your money is invested if you wish to, from a range of investments that USS offers or USS can invest these for you. For the defined benefit (DB) part, the Retirement Income Builder, USS makes those investment decisions on behalf of all members so that you receive your specific level of benefit. We're going to have a look at these in more detail now and show some examples of how the benefits are calculated.

In USS, everyone builds up Retirement Income Builder, defined benefit (DB) benefits, on their salary up to the salary threshold. And the salary threshold from 1 April 2026 is £74,208. If you earn above the salary threshold, then you'll also build up Investment Builder savings, or defined contribution (DC) savings, on



your salary above that threshold. If your earnings fluctuate around the salary threshold, any contributions to the Investment Builder section will stop and restart as appropriate automatically.

Now just having a closer look at how the Retirement Income Builder works. In the Retirement Income Builder, you build up a block of pension equal to a 75th of your salary for each year that you're a member of the scheme. The salary used in this formula though is only up to a maximum of the salary threshold, which is currently £74,208. So you will build up a block of pension for each year that you're paying into the scheme.

Then annual increases are applied to the block of pension between the time it's earned and the time it's eventually paid. These increases are currently linked to the Consumer Prices Index or CPI measure of inflation up to certain limits. If we add all those blocks together with those annual increases, we get your total annual pension. You'll also get a tax-free cash lump sum of three times your total annual pension, which is a one-off payment paid at the point of retirement paid in addition to your annual pension.

You can exchange some of your pension for a higher tax-free cash lump sum on retirement and vice versa, so you could even take no tax-free cash and take a higher pension for life. You make that decision when you come to retire.

Then once in payment, your pension will increase each year. Again these increases are currently linked to the Consumer Prices Index, or CPI measure of inflation up to certain limits. So that you can keep a track of how much you're building up, you'll receive details from USS each year in an Annual Member Statement which can be accessed on the member portal My USS.

Now just having a look at how the Investment Builder works. If you're earning above the salary threshold, then 20% of the value of your salary above this threshold is paid into the Investment Builder. This comes from the contributions that you and your employer are already paying in to USS and it's at no further cost to you. The contribution rate that you pay is 6.1% of your total salary.

We'll now have a look at your contributions and tax relief. You'll get tax relief on the contributions that you pay in to USS, meaning that your contributions are tax free. That means that some of the money that would normally go to the government in tax goes towards funding your pension instead. For example, if you're a basic rate taxpayer and you had £100 that was paid to you as salary, then 20% of this would be paid as tax and then you'd be left with £80 in your take home pay.

However if you put that £100 of your monthly wage into your pension, then that 20% that would usually be taken as tax is put into your pension instead. As your contributions are taken from your pay packet before you're taxed, you only pay income tax on the remainder of your wage. There are some limits to tax relief set by HMRC that you will need to be aware of while you're contributing to your pension, and these are particularly relevant if you're a high earner.

For example whilst you're paying in to USS, you could be affected by what's known as the Annual Allowance, particularly if you are a high earner now. The Annual Allowance is the maximum amount of pension savings you can build up each year before you get a tax charge, and the Annual Allowance for the current tax year is £60,000. You can find more detail on the Annual Allowance on the pension tax pages of



the USS website. Or you could register for our **Focus on pensions tax webinar** where we cover the Annual Allowance in more detail.

I've mentioned that you get tax relief on your contributions, but what are you and your employer actually paying in to USS? You as a member pay 6.1% of your total salary, so regardless of whether you're earning above or below the salary threshold in to USS. And your employer pays 14.5%. This goes towards paying all of your benefits from the scheme, so not just your pension benefits but also the life cover and the running costs of the scheme.

Saving into a pension scheme like USS can be tax efficient. You do not pay income tax on your pension contributions so that means the impact of your pension contributions on your take home pay is actually less than 6.1% of your salary. I've got some examples here to show you. First let's look at the example of someone who earns £25,000 a year and so pays income tax at the rate of 20%.

Their 6.1% contribution to USS amounts to £1,525 over a full year. But the impact on take home pay is just £1,220. That means there's an annual tax saving of £305. Using the Retirement Income Builder formula that we've been through before of building up a block of annual pension of a 75th of yearly earnings, this member will have built up a pension block of £333 a year. This is the amount that will be payable to the member in retirement, plus any annual increases for the rest of their life.

The member is also entitled to a tax-free cash lump sum of three times their pension at retirement. So for this member it's an additional cash sum of £1,000. At first glance you might think £333 does not look much compared to the contributions that have been paid in over the year. However, that £333 is an annual amount payable for the rest of that person's life, in addition to any valuable benefits payable after they've died as well.

Then we have an example of someone who earns £40,000, so is also paying income tax at the rate of 20%. Their 6.1% contribution to USS amounts to £2,440 over a full year, but the impact on take home pay in this case is £1,952. Using the formula again, this provides a pension block of £533 a year and a tax-free cash lump sum of three times the pension of £1,600.

Finally we have an example who earns £55,000 a year and is paying income tax at a rate of 40%, assuming they're not in Scotland. Their 6.1% contribution to USS amounts to £3,355 over a full year, but the impact on take home pay is just £2,013. This will provide a pension block of £733 and a tax-free cash lump sum of three times the annual pension at retirement of £2,200.

Also you might be able to pay your contributions through what's known as salary sacrifice if your employer offers it. It does go by some other names, but salary sacrifice means that your employer pays your contributions on your behalf and reduces your salary accordingly. So as well as not paying income tax on your pension contributions, you'll also save on National Insurance contributions because your salary is reduced before National Insurance is worked out.

The impact on your take home pay, if you're paying by salary sacrifice, might be even less than what I've shown on the screen here. As this salary sacrifice is operated through your employment contract, you would need to check with your employer whether salary sacrifice is available to you and if your contributions are being paid in this way.



To see an estimate of what the actual cost of your contributions might be, you can use the Contributions & Tax Calculator tool in My USS. Once you're in My USS, you can click on the Contributions & Tax Calculator tool here. Our example number has a salary of £25,000 and they are using salary sacrifice. The first thing we need to do is click the button here that says **Contributions are being paid by salary sacrifice** and then we can use the calculator to show the actual cost to the member, and also the employer contribution that's being paid on their behalf. So if we click here, we'll get your results.

You can see for this member earning £25,000 a year and paying contributions via salary sacrifice, their 6.1% monthly contribution is £127 but the actual cost to them is just £92. This section is about paying tax once your benefits come into payment. Once you retire and take your benefits you'll get an income for life and a one-off tax-free (up to certain limits) cash lump sum of three times your pension. You can choose to have a lower monthly income and a higher cash sum, or vice versa; it's up to you.

There is a limit though on the amount of benefits that can be taken as tax-free cash and USS will tell you this limit when they send you your retirement quote. Your benefit options on retirement, including pension and lump sum options, are covered in more detail in the **Approaching retirement webinar**. You may be taxed on the monthly pension income that you receive depending on the total level of your income. Your tax code is provided by HMRC and it'll be used to calculate the tax payable on your income in retirement.

The amount of income tax you pay on your USS benefits will also be determined by any income you earn from other sources. You'll generally pay income tax if your total annual income adds up to more than your personal allowance.

This income could include any State Pension that you receive, a private pension such as a personal pension or workplace pension like the one you've built up with USS. It could be employment or self-employment earnings and any taxable benefits that you receive, or any other income that you might receive from sources such as savings, investments or property.

In 2026/27, the personal allowance is set at £12,570 a year, or £1,084 a month. For anything you earn over and above your personal allowance, you'll be charged the relevant tax rate. Again, this depends on your total income. For the basic rate, which is currently between £12,571 and £50,270, you'll be charged 20% tax.

For the higher rate, which is anything between £50,271 and £125,140, you'll be charged 40% tax. For the additional rate, which is anything above £125,140, you'll pay 45% tax. Now the rates are slightly different in Scotland. Note that if your income is above £100,000 a year, your personal allowance actually reduces by £1 for every £2 that your income is over £100,000.

That means that your personal allowance is therefore £0 if your income is £125,140 or above, and so you would pay tax on that first £12,570 of earnings as well. For simplicity, all our examples assume that the member has that full personal allowance.

Let's first look at the example of someone who's receiving the full State Pension, which is £12,547 a year and pension from the USS of £12,453 a year. This brings their total income from all sources to £25,000 a



year and so they pay income tax at a rate of 20% level of income. Their remaining income is £12,430 and they would pay the 20% tax on this amount which is £2,486. That means their total tax payable is £2,486.

We've also got the example of someone who has a full State Pension, again of £12,547 a year. This time a pension from USS of £42,453 a year. They receive an income of £55,000 a year and therefore they're paying income tax at a rate of 40%, again assuming they're not in Scotland. Their personal allowance is £12,570 and they would not pay tax on that level of income. Their income between £12,571 and £50,270 is £37,700 and they would pay 20% tax on this which amounts to £7,540. Their remaining income is £4,730 and they would pay 40% tax on this which is £1,892 tax. That means their total tax payable is £9,432.

HMRC uses tax codes to tell your employer or pension provider how much personal allowance that you have to use on that income. Depending on how much of your personal allowance you're using from other sources, you may not receive all of your personal allowance on your USS pension.

But until HMRC issues a notification of a new tax code for your pension, USS might need to use an emergency tax code. The emergency tax code assumes that you have the full £12,570 personal allowance available. But that could result in a member paying too much or too little tax as it does not make any allowance for when in the tax year the payment actually starts, or what other income a member may have.

Once your new tax code is confirmed by HMRC and in place, any adjustments will be made to your income tax. It's also useful to be aware that starting to receive any new pension or cash payments that impact your taxable income levels might push you into a higher tax band. Or it might have an impact on your tax-free personal allowance, or it might mean that you need to complete a Self Assessment tax return.

Here we'll look at the calculators and tools that you can use to understand more about what you're paying in to USS and what your benefits and savings could look like when you retire. USS has calculators and tools online which can tell you more about things like the cost to you of contributing, how much you can save in tax relief, how much you could get in the future, or the impact of different options that you might choose from.

If you have not yet joined the scheme, you can use a basic calculator on the USS website, [uss.co.uk](http://uss.co.uk), to get a quick estimate of how much it could cost you to be a member and what you could get from USS at retirement. You'll find this basic calculator on the what your pension might look like page and that's in that you're a new joiner section of the area on the USS website For members.

In here all you'll need to do is input your date of birth and salary to be able to get that basic calculation of your how much it would cost you and what your benefits might look like at retirement. If you've already joined USS though or you've paid into the scheme in the past, you can log in to the online member portal My USS to use more detailed calculators.

You'll find that the calculators in My USS feature some prepopulated information because you'll be logged into your personal account. However, some calculators can be tailored to help you understand the impact of any decisions or changes you might make.



If you're thinking of contributing more of your salary in to USS or you've previously built-up benefits and you're thinking about paying in again, you might find the Contributions & Tax Calculator useful. There's also the Benefit Calculator.

This can help you understand what your benefits could look like in the future so whether you're paying in, whether you've got benefits and savings in USS but you're no longer paying in, or even if you've retired but you still have some savings in the Investment Builder and you want to see what they might look like. More information about using the Benefit Calculator, including a summary of what it can do with an explanation of each step, can be found on the Benefit Calculator section in My USS.

Here I'm going to show you the Contributions & Tax Calculator. The Contributions & Tax Calculator in My USS will already be prepopulated with your current information, and it'll have things like contributions and benefits in there as well.

You can factor in any additional contributions that you're thinking of paying into the Investment Builder and you can estimate how much you'll contribute and how much you'll save in tax. You can also see how much you could save in National Insurance with salary sacrifice if your employer offers this, and you can also see how much your employer will contribute to your future as well.

For this member, we're going to click here to get the results. This member on this example is earning £25,000 a year, they're paying contributions via salary sacrifice so their 6.1% monthly contribution works out to be £127, but the actual cost to the member is just £92 because they save on income tax and National Insurance contributions.

You can also use the Contributions & Tax Calculator to look at a **tax modelling** section to see how the Annual Allowance, the Tapered Annual Allowance and Money Purchase Annual Allowance could affect you, particularly if you're a higher earner. These allowances, set by HMRC, limit how much tax relief you can receive when building up benefits each year before you might need to pay a tax charge. You can find out more about these allowances on the pension tax pages of the USS website.

There's also, as mentioned, the Benefit Calculator in My USS. When you go into the calculator, you can either do a projection of your benefits into the future, or if you've had a retirement quote, you can use your figures to see what your options are on retirement, things like the combinations of pension and cash. But we'll just go into the projection tool here.

In here, the Benefit Calculator can be used to get an instant estimate of what you could get in the future, so it can be helpful at various stages throughout your journey with USS. And as mentioned, it will all already be prepopulated with some of your information.

Once you're in the calculator, if you scroll down the page, you can use it to make quick changes to things like your salary and age that you want to retire at to see what impact that has on your estimated benefits. But you can also make further changes to look at the impact and what that might do to your benefits by clicking this **View options** button here.

If we go in there; in here you can also model how making changes like saving more, transferring in, leaving USS, taking a career break or taking flexible retirement could impact what you get. And if you've got



Investment Builder savings, and that's whether you're still paying in, whether you're no longer paying in or whether you've retired, you can estimate what these savings would look like in the future and the options that you have to take them, including changing the level of tax-free cash lump sum you might take at retirement and the impact that might have on your pension income.