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An introduction to pension tax

Tax relief

Pension tax has become an important matter for a significant number of members of the scheme. The government has made changes to the maximum amount of pension savings that qualify for tax relief (generally to lower the thresholds), and a greater number of members are incurring, or at risk of incurring, pension tax charges. The limits apply to all of your pension savings into registered pension schemes and therefore you will need to consider your savings/benefits in other pension schemes, as well as USS.

This is no longer just a matter for the very highest of earners.

This section contains the information you will need to help you understand the limits on benefits you can accrue before you may incur a tax charge, how those limits work and what options you have to help you to manage your pensions tax affairs.

Pension tax is now part of the framework within which pension schemes have to work and although you may incur tax charges as you accrue benefits (as well as when you draw them) the scheme remains an extremely beneficial way in which to save for your retirement.

The resources available on this page will explain pension tax in detail, but set out below is a brief overview.

Tax relief and tax free cash

All of your contributions to the scheme, including any additional voluntary contributions, are currently eligible for tax relief at the highest rate of tax that you pay (subject to the limits explained below).

Read more about tax relief and tax free cash here.

That makes your contributions incredibly valuable. Of course, your pension benefits will be subject to tax when they are paid in retirement via the PAYE system. However you will have received the tax relief up front, plus if your marginal rate of tax in employment is greater than it is in retirement, that has a further positive effect overall.

For example, a higher rate tax payer benefits from tax relief of 40% today, but could pay just 20% income tax in retirement. This is an advantage of pensions over other forms of retirement saving where the income tax applies now rather than during retirement (such as an ISA).

When you retire, or draw your benefits, under current tax legislation, you have the option to draw up to 25% of the total value of your benefits as a tax free lump sum.

Are there any limits to how much I can build up?

The tax relief on your pension contributions and lump sum paid at retirement are generous concessions and there are limits to the amount you can build up tax-efficiently.

Read more about limits on building up here.

Currently, the two main limits, which apply across all registered pension schemes, are:

1. The Annual Allowance, which limits the tax relief you can receive on pension savings in a single year; and
2. The Lifetime Allowance, which limits the total amount of tax-advantaged retirement benefits that you can build up over the course of your working life.

Both of these limits are set by HM Revenue & Customs (HMRC).

Annual allowance (AA) - taxing benefit accrual

As an active member of USS, the amount of benefit you build up over a tax year is assessed against the AA.

Read more about Annual allowance (AA) here.

The calculation is assessed differently for defined contribution arrangements (the USS Investment Builder is a defined contribution arrangement) and for defined benefits arrangements (the USS Retirement Income Builder is a defined benefits arrangement).

The AA factsheet explains this measure in detail but essentially, should your pension savings across all pension schemes exceed the AA, you will be subject to a tax charge on the excess pension savings at your highest marginal rate.

You can pay the charge direct to HMRC or in certain cases you can ask USS to pay the charge via a facility called Scheme Pays. This is explained in the [Scheme Pays factsheet](#). You can also use any unused allowance from your previous three tax years to cover some or all of the excess.

The AA is £40,000 per annum from 6 April 2016, but this limit can be significantly reduced if your earnings are over a certain level, or if you have already drawn any benefits from a defined contribution arrangement (not just the USS Investment Builder).

Lifetime allowance (LTA) – taxing benefits when you draw them

At retirement, the total amount of benefits you have accrued in USS (plus all other registered pension schemes) is assessed against the LTA.

Read more about Lifetime allowance (LTA) here.

If your benefits exceed the LTA then there is a charge to pay which the scheme must satisfy before your benefits can be paid. This charge will be paid in the form of a reduction to the benefits that are in excess of the LTA.

The lifetime allowance is £1,030,000 from 6 April 2018, although some people may have protection from HMRC which gives them a higher LTA.

Options to help manage pensions tax

You do have choices and even when taking into account the tax implications, you may be better off remaining as a member of the pension scheme. However, the choice is yours and individual circumstances can make a material difference to the appropriate course of action.

Read more about options to help manage pension tax here.

If you are affected by pension tax, your options are: to remain as a member of the scheme; to withdraw entirely, or to consider one of the two USS specific options the scheme has made available for members to assist with managing their tax affairs, as follows:

- Enhanced Opt-Out (EEO) – which allows you to retain your death in service and incapacity cover without building up any further benefits; or
- Voluntary Salary Cap (VSC) – which allows you to apply a cap to your salary for pension purposes, so long as it is no lower than the salary threshold (£57,216.50 for 2018/19 and is revalued every year).

Full information on these allowances and scheme options available to you can be found in the following USS factsheets;

- [Lifetime allowance](#);
- [Annual allowance](#);
- [Scheme Pays](#);
- [Enhanced Opt-Out](#);
- [Voluntary Salary Cap](#);
- [Tax free cash at retirement](#);
- [Tax free cash options at retirement \(deferred members\)](#);
- [Historical information and HMRC tax protections](#); or
- [Our pensions tax FAQ page](#).

Please note that pension tax is a complicated area, and you will need to carefully consider the choices you make in relation to your pension savings (including any pension arrangements outside of USS). As previously highlighted, your net benefits, even after a potential tax charge, may be greater than the net cost of the contribution paid by you. However, neither the trustee company nor your employer can give you financial advice and you must make a decision based upon your own personal circumstances, and in doing so, you may wish to seek independent financial advice. You can find an independent financial adviser through the following website: www.unbiased.co.uk. Please be aware that you may be charged a fee for any advice.

If you've already reviewed your options and decided you wish to use a scheme option (EEO or VSC) to manage your pensions tax, you will need to complete the relevant form. Your employer has access to the voluntary salary cap election form, and you can download the enhanced opt-out form using the link below:

- [Election for enhanced opt-out with continued death and incapacity benefits](#)

Financial advice

Pension Wise – if you need some impartial guidance about the options you have with the USS Investment Builder and are aged over 50 you can contact Pension Wise – either by telephone: 0800 138 3944 or online at: www.pensionwise.gov.uk.

Read more about financial advice here.

Pension Wise is a free and impartial government service set up to give you guidance on your options under defined contribution schemes, like the USS Investment Builder. Pension Wise is accessible face-to-face, over the telephone or online.

You should consider taking independent financial advice in order to help you decide the most suitable option. You can find an independent financial adviser through the following website: www.unbiased.co.uk. Please note that you may be charged a fee for any advice.

Pension Wise will not be able to assist you with advice on your benefits from the USS Retirement Income Builder.

Your feedback

It is important that the trustee company understands the pension tax issues members face, and the information on this page is under regular review to ensure it remains relevant and helpful.

Your feedback is welcomed both in terms of the information available, and any additional information which would help you in your task of trying to decide how best to address any tax issues.

Please do submit your feedback via the [contact us form](#).

[PDF Print](#)

Related information

[Pension tax articles](#) [Pension tax relief in a nutshell](#) [The easy way to keep track of your annual and lifetime allowances](#) [The USS pension tax relief checklist](#) [A close look at pension tax FAQs](#) [Pension tax FAQs](#) [Tax FAQs for US citizen members](#) [Factsheets](#) [Lifetime allowance](#) [Annual allowance](#) [Scheme Pays](#) [Enhanced opt-out](#) [Voluntary salary cap](#) [Tax free cash at retirement](#) [Tax free cash options at retirement \(deferred members\)](#) [Historical information and HMRC tax protections](#) [Terms & conditions](#) [Privacy policy](#) [About cookies](#) [Contact us](#) [News](#) [Glossary](#) [Career opportunities](#) [Financial advisers](#)

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