Money Wise UK®

Growing together, with integrity and respect

ManningGee Investments

Sustaining Wealth and Trust



Pensions vs ISAs: Which Is Better? A Plain-English Explanation

Understanding tax, flexibility and how to make the most of both.

mgi-ifa.co.uk

Introduction

We are now entering the final part of our financial education series. This is Guide 10, where we consider one of the most common questions in financial planning: should you save into a pension or an ISA?

Pensions regularly attract headlines. Whether the discussion concerns tax relief, tax-free cash, inheritance tax or changes to retirement rules, it can sometimes feel as though the benefits of pensions are being gradually reduced.

It is easy to read these headlines and wonder whether pensions are still worth having.

On the other hand, ISAs appear relatively simple. You pay money in, your savings or investments benefit from favourable tax treatment, and you can normally withdraw money without paying tax.

Does that make an ISA better?

Not necessarily.

The answer depends on what you are trying to achieve, when you might need the money and your personal tax position.

In this guide, we explore four important themes:

- Tax now versus tax later: Understanding how contributions and withdrawals are treated.
- Access versus discipline: The benefits and limitations of being able to access your money.
- Why the right answer changes over time: How your needs evolve throughout life.
- Income and life-stage considerations: How pensions and ISAs can work together, particularly in retirement.

Our aim is not to declare a winner. Instead, we want to help you understand the choices so you can make informed decisions with greater confidence.

Where we have come from and where we are going

Our education series started with cash and the importance of having a financial foundation.

We then explored ISAs and pensions before moving on to investments, investment funds, active and passive investing, and the relationship between risk and return.

More recently, we considered market falls and how to invest when the future is uncertain.

Throughout these guides, we have returned to one important principle: financial decisions should support what you want to achieve in life.

We now move into the final section of the series, where we bring these ideas together and explore the decisions and trade-offs we all face.

Next month, we will consider the starting dilemma: how do you decide what to do first? We will then conclude the series with a simple framework for managing your money.

Going back to the beginning: Understanding the difference

One of the most important things to understand is that an ISA and a pension are not investments themselves.

They are often described as tax wrappers.

Think of a wrapper as a container that holds your money and investments. The container determines the tax rules, while what you put inside determines how the money behaves.

Depending on the type of pension or ISA, the underlying assets might include cash, investment funds, company shares, government bonds or corporate bonds.

For example, you could hold the same global investment fund within a Stocks and Shares ISA and a pension.

The investment risk and potential return would be broadly the same, assuming identical holdings and charges.

However, the tax treatment and access rules would be different.

The wrapper and the investment are two separate decisions.

Understanding this distinction helps prevent a common misunderstanding: that pensions are inherently riskier than ISAs, or vice versa.

Neither is necessarily true.

How does a pension work?

We have covered pensions in an earlier guide, but it is worth revisiting the main features.

A pension is designed primarily to help you build money for retirement.

Its main advantages include:

- Personal contributions can normally benefit from tax relief, subject to eligibility and allowances.
- Your employer may also contribute, providing additional money towards your retirement.
- Investments within a pension generally grow free from UK income tax and capital gains tax.
- You can normally take up to 25% of eligible pension benefits tax-free, subject to the relevant limits and rules.

However, there are restrictions.

For most people, pension money cannot normally be accessed until age 55, increasing to 57 from April 2028, unless an exception applies.

In addition, withdrawals beyond the tax-free element are normally subject to income tax.

This means that while pensions can be very tax-efficient when saving, it is important to consider how you will take the money out.

How does an ISA work?

An ISA works differently.

You contribute money that has generally already been subject to tax. There is no income tax relief when you pay money into an ISA.

However, once the money is inside the ISA:

- Interest, investment income and capital gains are normally free from UK tax.
- Withdrawals are normally tax-free.
- You can generally access your money when you need it, although some products have restrictions or charges.
- ISA income and gains normally do not need to be included on your tax return.

There are different types of ISA.

A Cash ISA holds cash-based savings, while a Stocks and Shares ISA can hold investments.

For this comparison, we are primarily considering adult Stocks and Shares ISAs, although the tax and access principles also apply broadly to Cash ISAs.

The important difference is that an ISA offers flexibility.

You could use the money towards a house deposit, to support your family, to fund an unexpected expense or to supplement your retirement income.

But flexibility also means responsibility. Money that is easily accessible can be spent before it is needed for longer-term goals.

A simple comparison

Area	Pension	ISA
Tax relief on contributions	Normally available	Not available
Employer contributions	May be available	Not available
Tax while invested	Generally tax-efficient	Generally tax-efficient
Access	Normally restricted by age	Normally available at any time
Tax on withdrawals	Part may be tax-free: the balance normally taxable	Normally tax-free
Contribution limits	Pension allowances and earnings rules apply	ISA allowance applies
Effect on taxable income	Withdrawals may increase taxable income	Withdrawals normally do not
Treatment on death	Depends on pension and inheritance tax rules	Normally forms part of estate, with some spouse/civil partner benefits
Main strength	Tax-efficient retirement saving	Flexible, tax-free access

Both have advantages. Both have limitations.
The interesting question is what happens when we start to look at the numbers.

Tax now versus tax later

One of the biggest differences between pensions and ISAs is when you receive the tax benefit.

With a pension, you can normally benefit from tax relief when you contribute. However, you may pay income tax when you withdraw the money.

With an ISA, you do not receive tax relief when contributing, but withdrawals are normally tax-free.

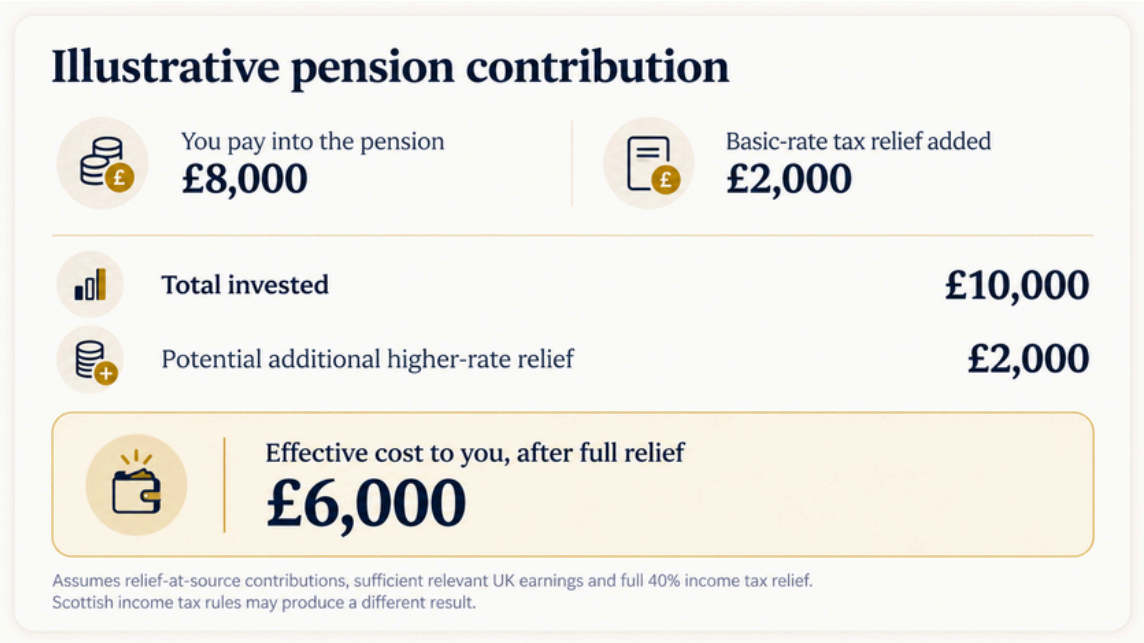
This creates an interesting question.

Would you rather receive tax relief today or have tax-free access in the future?

The answer depends partly on your tax position now and what you expect it to be later.

An example: The value of pension tax relief

Imagine you are a higher-rate taxpayer and want to invest £10,000 into a personal pension.



This means that £10,000 could be invested in your pension at an effective cost of £6,000.

However, this is only part of the story.

When you eventually withdraw the money, some or all of it may be subject to income tax.

If you pay a lower rate of tax in retirement than you did while working, the pension could offer an additional advantage.

But if you are paying the same or a higher rate of tax when withdrawing the money, the comparison changes.

What difference could investment growth make?

Assume the same investments grow by 5% a year over 20 years, before fees and tax.
Illustrative investment growth over 20 years

Assumes 5% annual compound growth, before fees and withdrawal tax.



Illustration assumes the same £6,000 effective personal cost, full pension tax relief, and identical investment returns. It is not a comparison of after-tax retirement proceeds.



The pension starts with a larger amount because of the tax relief.

However, we cannot conclude that the pension is automatically better. We must also consider the tax payable when money comes out.

This is why financial planning considers the full journey, rather than just the initial tax saving.

What about employer contributions?

For employees, this can be one of the strongest arguments for pension saving.

Many employers contribute towards their employees' pensions, and some offer more generous contributions when employees increase their own payments.

For example, an employee might contribute £100 and receive an additional £100 from their employer, depending on the scheme.

This is additional money towards retirement that would not normally be available through an ISA.

Before choosing an ISA instead of a workplace pension, it is worth understanding what employer contributions you might be giving up.

Access versus discipline

One of the biggest strengths of an ISA is that you can normally access the money whenever you need it.

But could that also be a weakness?

Consider someone in their thirties who wants to save for retirement but also expects to move house, help their children or perhaps take a career break.

An ISA offers flexibility.

If their circumstances change, the money is available.

However, if the money is intended for retirement, the temptation to withdraw it for other purposes could reduce what they have available later.

A pension works differently.

Because access is normally restricted until the minimum pension age, it encourages long-term saving.

For some people, that restriction is helpful. For others, particularly those who might need the money earlier, it can be a disadvantage.

Neither approach is right for everyone.

The important consideration is whether you need access to the money before retirement.

A useful starting point is to separate money into different purposes: emergency savings, medium-term goals and long-term retirement savings.

An ISA and a pension can then play different roles within that plan.

Why the right answer changes over time

Financial planning is not a decision you make once and never revisit.

Your priorities at 25 are likely to be different from those at 45, 60 or 75.

Consider how the role of pensions and ISAs might change.

Early working life

Building an emergency fund, managing debt and saving for a first home may be priorities. Workplace pension contributions remain important, particularly where an employer contributes. An ISA, or a Lifetime ISA where eligible, may support other goals.

Building a family and career

Mortgage commitments, childcare and education costs can create competing demands. ISAs may offer flexibility while pensions continue building retirement savings.

Approaching retirement

Pension tax relief may become particularly valuable during higher-earning years. However, ISA savings can provide options for reducing working hours or retiring before pension benefits become accessible.

During retirement

The focus moves from building wealth to using it. Pensions, ISAs and other savings may work together to provide sustainable, tax-efficient income.

These are examples rather than fixed rules.

Someone in their twenties might be focused entirely on retirement, while someone in their sixties may still be building wealth or supporting their children.
The right approach starts with the individual, not their age.

.

How pensions and ISAs can work together in retirement

This is where the comparison becomes particularly interesting.

When we save for retirement, we often concentrate on how much money we can accumulate.

But retirement brings a different question.

How do we turn that money into income, while managing tax and keeping enough flexibility for the future?

Pensions and ISAs can complement one another.

Pension withdrawals may increase your taxable income, whereas ISA withdrawals normally do not.

This means an ISA can help meet additional spending needs without necessarily pushing you into a higher income tax band.

An example: Funding an additional £10,000

Imagine someone in retirement receives £25,000 a year from their State Pension and other taxable pension income.

They would like an additional £10,000 for a holiday and home improvements.

They have two possible sources of money.



This does not mean the ISA should always be used first.

For example, someone may have unused personal allowance or basic-rate tax band available. Taking pension income could then be appropriate.

There may also be reasons to preserve ISA savings for future needs.

The important point is that having different sources of money gives you more choices.

Retirement income is not always the same each year

Some years, spending may be relatively predictable.

Other years, you might want to replace a car, help a family member, travel or make improvements to your home.

A financial plan can distinguish between essential expenditure, discretionary spending and one-off costs.

Pension income might meet regular spending needs, while ISAs and cash could help with larger or unexpected expenses.

The precise combination depends on your circumstances, investment risk, tax position and long-term needs.

What about inheritance tax and passing on wealth?

This is an important area because the rules surrounding pensions and inheritance tax are changing.

Historically, many pensions have benefited from favourable inheritance tax treatment, making them attractive not only for retirement income but also for passing on wealth.

The government has legislated for most unused pension funds and certain death benefits to be brought within the scope of inheritance tax from 6 April 2027.

This does not mean pensions automatically become unattractive.

Pensions can still provide valuable tax relief, employer contributions and tax-efficient investment growth.

However, it does mean that the decision to preserve a pension while spending other assets should not be based solely on historic inheritance tax advantages.

ISAs generally form part of an individual's estate for inheritance tax purposes. There are also special rules for surviving spouses and civil partners, including additional permitted ISA subscriptions.

For both pensions and ISAs, the outcome on death depends on individual circumstances, beneficiary arrangements and the tax rules at the time.
The wider message is that retirement planning and estate planning are closely connected.

It is important to consider not just how to build wealth, but how to use it, protect it and eventually pass it on.

What about business owners?

For business owners, pensions can offer additional opportunities.

Depending on the business structure and circumstances, employer pension contributions may provide a tax-efficient way to build retirement savings.

For example, a limited company may make pension contributions on behalf of a director, potentially reducing its corporation tax liability where the relevant conditions are met.

However, pension annual allowances, tax rules and the company's circumstances must all be considered.

An ISA can still play an important role by providing personally accessible savings outside the business.

For business owners, having money available can be particularly valuable when income fluctuates or business opportunities arise.

Once again, the choice is not necessarily between a pension and an ISA.

It is about finding a suitable balance between retirement saving, personal flexibility and business needs.

Bringing everything together: A simple decision framework

Rather than asking whether a pension or an ISA is better, it can help to ask a few questions about what you want your money to achieve.

When might I need the money?

Money needed before pension access age may be better suited to accessible savings or ISAs.

Am I receiving the full benefit of employer pension contributions?

Employer contributions can make workplace pension saving particularly valuable.

What tax do I pay today, and what might I pay in retirement?

Tax relief on contributions and tax on future withdrawals both affect the outcome.

Do I have enough accessible savings?

Keeping money available for emergencies and changing circumstances can help protect a long-term financial plan.

How will I use the money in retirement?

A combination of taxable pension income and tax-free ISA withdrawals may provide more flexibility.

What do I want to leave to my family?

The screenshot only shows the beginning of this question, so the accompanying explanation isn't visible.

There is no single answer that works for everyone.

Your income, age, family circumstances, retirement goals and attitude towards risk all influence the decisions you make.

It is also worth remembering that the answer can change. A strategy that works today may need adjusting as your circumstances develop.

Our final thoughts: Better together?

We started this guide by asking a simple question: is a pension or an ISA better?

Hopefully, the answer is now clearer.

Pensions offer valuable tax relief, potential employer contributions and a structured way to save for retirement.

ISAs provide tax-efficient investment growth, tax-free withdrawals and flexibility over when you can access your money.

Both have limitations.

A pension restricts access and may create an income tax liability when money is withdrawn.

An ISA provides no tax relief on contributions, and easy access can make it tempting to spend money intended for the future.

But perhaps the biggest lesson is that we do not always need to choose one over the other.

A pension can help you build retirement wealth. An ISA can help you retain flexibility. Together, they can give you more choices about how and when to use your money.

At Manning Gee Investments, we believe good financial planning starts with understanding what matters to you.

The investments and tax wrappers come afterwards.

The aim is not simply to pay the least amount of tax today. It is to build a financial plan that supports your life, adapts as circumstances change and helps you make confident decisions about your future.

What comes next?

In Guide 11, we will explore the starting dilemma.

You may understand the benefits of cash, ISAs, pensions and investments, but how do you decide what to do first?

Should you repay debt, build cash savings, contribute more to your pension or invest through an ISA?

We will explore how to prioritise these decisions before bringing the whole education series together in Guide 12.

Contact:

0117 427 0495 naomi.gee@mgi-ifa.co.uk mgi-ifa.co.uk

Manning Gee Investments Limited is authorised and regulated by the Financial Conduct Authority. FCA Number 844546. Registered in England and Wales under Company Number 11968984, it has its Registered Office at 27 Old Gloucester Street, London, WC1N 3AX.

General disclaimer:
The information in this financial education guide is for general educational purposes only and should not be considered personal financial advice.

We source some data from external providers. While we aim to ensure the information is accurate and up to date, we cannot guarantee the accuracy or completeness of information provided by third parties.

This guide is based on UK tax rules and legislation as at October 2026, which may change in the future and may affect the information provided.

Anyone considering a financial product or service should seek professional advice or carry out their own research before making any decisions.

Investments can fall as well as rise and returns are not guaranteed. You may get back less than you originally invested.