CURTIS BANKS

CASE STUDY

CARRY FORWARD

APPROVED FOR ADVISER USE ONLY | APRIL 2023

This case study is from Meet the Joneses – Series 2. This series is set 4 years after Series 1. Information about the family and further case studies can be found on our website, www.curtisbanks.co.uk/meet-the-joneses. All characters in the Jones family are fictional and intended for demonstrative purposes only.

The Challenges

Dan Jones is 54 and has an income of £75,000. He's financially comfortable, but is the first to admit that his pension hasn't been his biggest priority throughout his career, and isn't quite where he'd like it to be.

That said, over the last few years Dan has been making an effort to save more. When his mother Margaret died four years ago, he used some of the money he inherited at the time to contribute £70,000. Since then, he has been contributing £15,000 a year as a mix of personal and employer contributions using his company's generous matched contributions scheme. Dan keeps meaning to increase his personal contributions, but never quite gets around to it.

When Margaret died, she had recently gone into some fixed term investments that have recently matured, and Dan has received a further £60,000. It's prompted him to consider making another larger contribution to his pension and revising his personal contributions.

Dan is only vaguely aware of tax relief and the annual allowance rules. When he made his larger contribution four years ago, his daughter Paula, who had been researching the rules for her own purposes at the time, had assured him that it was fine.

Dan remembers Paula telling him something about 'carry forward' rules, but he can't really remember much about it. He decides to ask Paula for help again, and this time is determined to pay attention and learn the rules properly.

The Actions

Dan tells Paula that he'd like to contribute as much as he can now as a single lump sum, before updating his personal contributions ready for the new tax year. He's contributed £15,000 this year as normal.

Paula tells her father that strictly speaking he can pay as much as he likes into his pension, but there are limits on the amount of tax relief he can benefit from, which will probably determine how much he actually wants to contribute.

Paula explains that you can claim tax relief on personal contributions up to the value of your earnings each year. However, if you exceed the annual allowance, you will have to pay an annual allowance charge, which is designed to effectively take back the tax relief on the funds which are in excess of the annual allowance. Paula confirms that the annual allowance is currently £60,000.

Dan is disappointed as he was hoping to contribute more. He also wonders if the annual allowance has gone down recently, or whether

Paula made a mistake four years ago when they talked about his £70,000 contribution.

Paula knows that the annual allowance has gone down in the past, but tells her father that this isn't the reason his £70,000 contribution didn't face a charge. She asks if he can remember her telling him about carry forward before. Dan sheepishly admits that all he can really remember is Paula telling him that the contribution would be fine.

Paula explains that while the annual allowance is £60,000, Dan can also use up unused allowance from previous tax years: this is what's known as carry forward. She pre-empts Dan's next question and confirms that it's only possible to go back to the previous three tax years using carry forward.

As the annual allowance has been £40,000 for the last three years and Dan has contributed £15,000 in each, he has £75,000 of carry forward available to add to this year's £60,000 allowance. Dan asks Paula if that's correct, as half of the annual £15,000 is from employer contributions. If the annual allowance is supposed to limit tax relief, shouldn't it only test personal contributions?

Paula says that it's definitely correct that employer contributions are also tested against the annual allowance. She'd always assumed it was because otherwise there would be an easy loophole: people could just ask their employers if they could give up salary in exchange for employer contributions and never have to worry about the annual allowance regardless of the amounts involved.

Dan's total available annual allowance for this year, including carry forward, is therefore £135,000 – of which he has already used £15,000 with his normal contributions. Dan had been planning to contribute the £60,000 he's just received, plus a further £20,000 from his savings that he thinks he would already have paid in, had he got around to updating his contributions sooner. He starts to consider whether he could afford to increase the contribution given that he has the carry forward available, but Paula points out that he's forgotten about the tax relief limit.

Dan might have the annual allowance to support £135,000 worth of contributions, but the tax relief Dan can claim on his personal contributions is still limited by his £75,000 income for this tax year. Therefore after the £7,500 he's already contributed, he can contribute a further £67,500 (including the tax relief). While Dan could pay in more and simply not receive any tax relief, Paula tells her dad that when she was in a similar position, she simply waited until the following tax year to contribute more so that she didn't miss out.

The Results

Dan decides to follow his daughter's lead, and contributes a further £67,500 gross, making his total for the year £82,500.

Dan had a further slight disappointment in learning that he couldn't attribute this to £75,000 worth of carry forward and £7,500 from the current year's allowance, in order to give himself as much time as possible to use the remaining allowance. Paula explained that in order to use carry forward, you have to use up the current year's allowance first. Therefore Dan has used up the current year's allowance, plus most of the allowance from 3 years ago. Dan makes a note to keep track of his carry forward allowance and to try to use it up in future tax years.

Important points to consider

The value of pension funds may fall as well as rise. Your money is tied up until you take your benefits. Benefits can generally be taken any time after age 55, although this is due to increase to 57 in 2028.

Contact details

If you'd like to speak to us about anything in this case study, please contact us on:

T 01473 296 950

We may record and monitor calls. Call charges will vary.

E enquiries@curtisbanks.co.uk

Please remember not to send any personal, financial or banking information via email as it is not a secure method of communication.