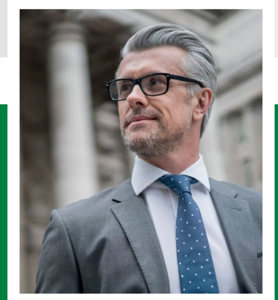
For financial advisers only

Quilter

Funding for high earners using carry forward now - Case Study



Michael, 55, a barrister, based in London.

Michael has just gone through a divorce after 25 years of marriage. This has had a big effect on his accumulated pension savings. Michael has re-evaluated his life. He has decided to retire in five years and needs solutions to maximise his retirement income. Ideally he'd like to leave London to move to a smaller house by the sea. Michael is a keen weekend sailor, and when he retires he would like to buy a slightly bigger yacht and go on longer trips. Michael has two children who live independently.

Michael's current retirement provisions

Michael has two main sources of retirement income: his personal pension and a number of residential properties he owns.

Michael hasn't made any contributions to his personal pension since 2005/06. Michael had originally registered his pension savings for Enhanced Protection. However, this was lost where, as a result of a divorce settlement his pension funds were severely reduced and so Michael revoked his protection and began pension contributions again. He would now like to carry on re-building those savings.

He has other investments in bank deposits, unit trusts and National Savings and in the current tax year he estimates his relevant earnings will be in the region of £400,000 (as they have been for the past four tax years) but is uncertain how much longer he will continue to generate that level of earnings as he winds down towards his planned retirement.

The freedoms as to how he could use pension savings to provide an income and the change to the tax regime on residual pension capital on death have focused Michael on how re-building his pension savings could provide a tax efficient solution to his longer term retirement plans.

His personal pension is invested in a managed fund which hasn't performed particularly well. The current pension has a maturity age of 75 at which time all benefits must be crystallised, and does not offer flexi-access drawdown as a retirement income option.

How can Michael use pension funding to achieve his objectives?

- Michael can make a personal contribution of up to 100% of his £400,000 UK relevant earnings but will likely want to keep his gross contribution within his available Annual Allowance.
- Michael's expected income for the current tax year will subject him to the tapered annual allowance rules, which, based on his expected income will limit the relievable annual allowance for the current tax year to £10,000.
- As tapered annual allowances have been in place since 2016/17, Michael needs to consider tapered annual allowances in earlier years as well as the current tax year.
- Michael needs to be aware that the tapered annual allowance limits were different in previous tax years
- He will receive tax relief on the contribution at his highest marginal rate by extension of his basic rate tax band.
- However, as Michael has not used any of his Annual Allowance in the three previous tax years, but has been a member of a registered scheme, he can carry these unused allowances forward to the current tax year.
- He can, through his financial adviser, use a new personal pension plan, such as the Collective Retirement Account to really maximise the tax advantages of available funding in this tax year.

How would the Collective Retirement Account deliver this solution for Michael?

Michael could make the maximum tax-advantaged contribution in the 2024/25 tax year of £28,000 (gross). To do so, he would need to:

- use this year's Annual Allowance (£10,000) and
- access all his unused carry forward from previous tax years (£10,000 from tax year 2023/24 and £4,000 tax year 21/22 and 22/23 giving a total carry forward of £18,000)

How does this planning help achieve Michael's retirement goals?

1. By applying this planning Michael has significantly reduced his income tax bill for the current tax year. He will benefit from £5,600 of basic rate tax relief at source and £7,000 of additional rate tax relief (difference between basic rate relief received and additional rate, so 25%), a total of £12,600.
If Michael's future income reduces below £260,000 in future years he will be subject to the normal annual allowance (currently £60,000) meaning he may increase his pension savings should he wish to do so.

2. By increasing his retirement fund, Michael increases his potential future tax-free cash lump sum – creating access to more of the capital he will need to buy his boat. He has at the same time increased the fund that will provide a retirement income which, with careful planning, may be taxed at a lower rate of income tax than the rate of relief on the additional contribution he is making.

3. Michael is able to pass on his entire retirement fund to his children if he dies before his 75th birthday, whether he has drawn on any of his savings or not and any such capital could be used to provide into a beneficiaries' drawdown arrangement. This would enable the children to access capital as a future income with no income tax charge being applied to those payments. If he dies after 75 with any pension savings remaining, that value can still be passed to his children although the payments will be subject to the beneficiaries' marginal rate of tax. Using the beneficiary drawdown facility may enable the children to reduce the effect of taxation by drawing income only as and when required, alongside any other income they have. The undrawn amounts will be invested in a pension fund, with a chance to grow outside of the children's IHT estate, and when the children die any unused funds may provide lump sum or beneficiary pension death benefits to their beneficiaries.

4. Alternatively he can use part, or all of his fund, after any payment of tax-free cash to secure a lifetime annuity to take account of future changes to his health.

5. The Collective Retirement Account provides flexible income solutions to deliver the outcomes Michael is looking for at no additional charge. This provides an opportunity for Michael and his adviser to also review whether his existing pension savings should be consolidated with the new investment to enable a more controlled and better managed retirement income plan, with longer term and more flexible income and legacy solutions.

Your clients' investments may fall or rise in value and they may not get back what they put in.

The tax treatment and efficiency of these options will depend on the individual circumstances of each customer. Tax rules and their application may change in the future.

quilter.com

Please be aware that calls and electronic communications may be recorded for monitoring, regulatory and training purposes and records are available for at least five years.
Quilter is the trading name of Quilter Investment Platform Limited which provides an Individual Savings Account (ISA), Junior ISA (JISA) and

Collective Investment Account (CIA) and Quilter Life & Pensions Limited which provides a Collective Retirement Account (CRA) and Collective Investment Bond (CIB).

Quilter Investment Platform Limited and Quilter Life & Pensions Limited are registered in England and Wales under numbers 1680071 and 4163431 respectively.

Registered Office at Senator House, 85 Queen Victoria Street, London, EC4V 4AB, United Kingdom. Quilter Investment Platform Limited is authorised and regulated by the Financial Conduct Authority. Quilter Life & Pensions Limited is authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority and the Prudential Regulation Authority. Their Financial Services register numbers are 165359 and 207977 respectively. VAT number 386 1301 59.

Published: May 2024

QIP 11122/107/6990