Sanlam Wealth

Sanlam Onshore Bond

SCENARIO 3: MAXED OUT ON PENSIONS

CASE STUDY

Exploring tax-efficient options for a client who is concerned their final salary pension may breach the pension lifetime allowance

Client details

- A divorced 57-year-old NHS orthopaedic consultant who also has a private practice.
- Higher rate tax payer.
- Has a non-dependent daughter from a previous marriage.
- Wants to retire in three years and is a member of the NHS final salary pension scheme.

Current assets	Value
Primary residence	£650,000 (mortgage free)
Holiday home in Spain	£250,000 (mortgage free), which they rent out for six months of the year.
Cash	£30,000
Investment account	£300,000
ISA	£200,000
Pension (defined benefit) current value	£950,000
Total	£2,380,000
Total subject to inheritance tax (IHT)	£1,430,000

Planning needs

- He is concerned the value of his final salary pension will breach the lifetime limit for pension savings.
- He wants to ensure his income is tax efficient.
- He is concerned about his current IHT liability.

Proposal

1. Keep the cash
Use as an emergency fund for unforeseen circumstances.

2. Sell the assets in the investment account
Capital Gains Tax might be due, but this would be at a maximum rate of 20% as higher rate tax payers compared to IHT at 40%. The client would also have a Capital Gains Tax annual exemption of £12,300 to set against any gains. While the client reinvests the dividend income, this is still chargeable to income tax at 32.5%.

3. Sell the ISA savings
While there are opportunities for IHT planning with ISAs holding AIM listed shares, it was agreed that this investment was deemed too high risk after completing a risk questionnaire.

4. Invest the proceeds from the investment account and ISA (£500,000) into an onshore bond
As IHT planning is a primary concern, this bond should be placed into trust to help reduce the IHT liability. The investment in the bond would be charged at 20% within the fund, (less than the income tax charged if left in the investment account). The type of trust will depend on the client's aims, whether he requires access to the money invested and who he wants to benefit. However as a trustee, he would maintain some control over this investment and who can benefit from it.

5. Discuss the final salary pension scheme
On the client's current level of salary and years service, he is more than likely to face tax charges for going over his lifetime allowance for pension savings. However, as this is an employer funded scheme, this benefit outweighs the tax he would pay and so it is recommended he remain a member of this scheme and continues to contribute and receive accruals.

6. Additional investment to the investment bond
As maximising income tax efficiency is also key for the client, his current salary is enough to maintain his standard of living, so the rental income he receives is to be periodically invested into the onshore bonds, to help reduce the IHT liability, subject to the trust allowing this.

Things to consider

- The residence nil rate band is now increased to £175,000 per person for tax year 2020/21.
- His estate administrators could claim the residence nil-rate band to reduce some of the IHT payable on the main residence subject to certain conditions being met.
- The client might retire abroad or reduce the amount of time he rents out his Spanish property.
- Regular reviews will be essential to ensure the client's retirement aims are met.

The results

Depending on the type of trust used, consideration should be given to the impact of the tax charges when the gift is made to trust, periodic tax charges and exit charges when the money is taken out.

- The client achieves, tax efficient savings while he is still working.
- While he will pay tax on the income taken over the lifetime allowance, the benefit to him outweighs this.
- Placing the bond in trust will help reduce the IHT liability and leave a legacy to his daughter.
- Tax deferred withdrawals can be taken from the bond in future years by the client, depending on the type of trust used.

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