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 one 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

- I am concerned my final salary pension will breach the lifetime limit for pension savings.
- I want to maximise my income tax efficiency.
- I am concerned about my 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 a higher rate tax payer compared to IHT at 40%. I also have an annual exemption of £11,700 for the 2018/19 tax year. I do not take income from this investment but the dividends paid are 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 too high risk for me.

4. Invest the proceeds from the investment account and ISA (£500,000) into an onshore bond
As IHT planning is a primary concern for me, this bond should be placed into trust to help reduce the IHT liability I have. The investment in the bond would be charged at 20% within the fund (less than the income tax charged if left in my investment account) until a chargeable event occurs. The type of trust will depend on my aims, whether I require access to this and who the beneficiaries will be, but I would be one of the trustees to retain some control of this money and how it would be distributed.

5. Discuss my final salary pension scheme
On my current level of salary and years of service, I could face tax charges for going over the lifetime limit for pensions savings. As this is an employer-funded scheme, the benefit I would receive would outweigh the tax I would pay going over my lifetime allowance. We decided that I will remain as a member of the scheme and continue with accruals and contributions.

6. Additional investment to the investment bond
As I want to maximise the tax efficiency of my income and I have enough income from my salary, the rental income I receive could be invested into my onshore bond periodically to reduce the size of my estate and hence IHT liability, subject to the trust allowing this.

Things to consider

- The residence nil rate band will increase by £25,000 each year until the 2020/21 tax year, when this, along with the standard nil-rate band, will increase in line with the consumer prices index.
- My daughter could claim the residence nil-rate band to reduce some of the IHT payable on my main residence, if inherited.
- I may retire abroad or reduce the amount of time I rent my property out once retired.
- Regular reviews will help plan for my retirement.

The results

Depending on the type of trust used, consideration should be given to the impact of any tax charges when the gift is made to the trust, periodic tax charges and exit charges when money is taken out of the trust and arrangements need to be made to cover these liabilities if applicable.

- I will make tax-efficient savings while I am still working.
- I will pay tax on income taken above the lifetime limit but the benefit of having these accruals will outweigh the tax I pay.
- The gift of the bond to trust will help reduce my IHT liability and leave a legacy to my daughter.
- I have the option to take tax-efficient income/lump sums from the bond in future years depending on the type of trust used.

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