Later Life Planning

Q&A Slides

2 Day Workshop

November 2019

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Dave, aged 67 and Sarah 59 are married. They jointly donate £200 per month to a cancer charity. The payment is made from their joint bank account and they have signed the appropriate gift aid declaration. The couple have the following assets and income:

Owner	Asset	Value	Gross Income in current tax year
Dave	State pension	N/A	£9,256
Dave	Self-invested Personal Pension (SIPP)	£900,000	£30,000 (see below)
Joint	Bank Accounts	£90,000	£450
Joint	Corporate Bond Unit Trusts	£300,000	£7,500
Dave	Share Portfolio	£570,000	£22,800
Dave	SJP ISA – Balanced Portfolio	£170,000	£5,950

Dave took a £30,000 gross uncrystallised funds pension lump sum (UFPLS) from his SIPP in July of the current tax year. Dave's share portfolio is comprised of a small number of UK based blue chip shares that he has researched and selected himself. They have performed very well and whilst he still has a keen interest in the markets, he has less time available to undertake the research required.

Calculate, showing all your workings, Dave's income tax liability for the current tax year. (15 Marks)

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Crunch The Numbers…..

	Non savings income (£)	Savings income (£)	Dividend income (£)
State pension	9,256		
UFPLS (£30,000 x 75%)	22,500		
Bank Acc (50%)		225	
Corp Bond UT (50%)		3,750	
Dividends			22,800
Total income	**31,756**	**3,975**	**22,800**
Personal allowance	(12,500)		
Income to be taxed	19,256	3,975	22,800

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Crunch The Numbers…..

Basic rate tax band = £37,500 + 50% of gift aid [(£2,400 x 50%) ÷ 0.8] = £39,000

Income tax payable

Non savings income £19,256 x 20% = £3,851.20

Savings income £3,975 - £500 PSA = £3,475 x 20% = £695

Dividend income £2,000 x 0% = £0

Balance of BRB = £39,000 – (£19,256 + £3,975* + £2,000*) = £13,769 x 7.5% = £1,032.68

Balance of Divs = (£22,800 – £13,769 - £2,000*) = £7,031 x 32.5% = £2,285.08

Total tax payable: £3,851.20 + £695 + £1,032.68 + £2,285.08 = £7,863.96

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Barbara, who has 2 daughters and is aged 62, is married to Jim, aged 63, where they both have a medium attitude to risk . Jim has a SIPP, which is currently valued at £850,000. He has taken a part time job on a salary of £35,000 per annum. He plans to retire fully when he reaches his State pension age (SPA) of 66. Barbara inherited a FAD plan in May 2015, following the death of her father, aged 81. Barbara has designated the fund, currently valued at £420,000, as a nominee's FAD. The fund is wholly invested in fixed interest funds as Barbara's father had been about to purchase an annuity when he died. As a result of Barbara's recent retirement, in May 2020, where her salary was £20,000, the couple require additional net income of £30,000 per annum to top up Jim's salary of £35,000. A summary of their assets is below:

Owner	Asset	Current value	Income received in current tax year
Joint	Current account	£20,000	N/a
Joint	Building society savings account	£70,000	£700
Joint	Blue chip share portfolio	£120,000	£7,200
Joint	FXD Corporate Bond Unit Trust	£125,000	£4,370
Barbara	Onshore investment bond	£160,000	N/a
Barbara	ISA – ABC UK Equity Growth Fund	£165,000	£1,750
Jim	SJP ISA – balanced portfolio	£127,000	£3,800

£90,000 was invested into the investment bond in May 2009. No withdrawals have been taken from the bond. The couple have a mortgage free property valued at £860,000 and they plan to sell this in the next couple of years and downsize ready for their retirement.

Detail and justify why you have recommended that this income should be taken from the couple's investment portfolio rather than from either of their pensions and any associated income tax advice (15 Marks)

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Strategy….

- Any income taken from the FAD is fully taxable at HMR as Barbara's father died after the age of 75
- Jim's SIPP could provide PCLS, but taking funds from their pensions will reduce their IHT exempt assets.
- They can take tax-free funds from the ISAs which will reduce the amount of funds that need to be used to provide the income required.
- They can encash some of the share portfolio in subsequent tax years as this will provide tax free income within their CGT exemptions.
- They have not taken any withdrawals from the bond and can therefore use the cumulative 5% of original capital invested allowance to provide a tax deferred income.
- They can switch more of the ownership of savings/shares/UTs into Barbara's name to make use of her personal allowance.
- They can switch investments into income funds to generate more income.
- Taking funds from the investment portfolio reduces their estate for IHT purposes and so reduces IHT on 2nd death. It also allows Barbara to leave her pension funds to her family.

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Income Tax Advice

- Utilise stocks and shares ISA allowance for both via existing collectives / feeder in 2020/21 / current tax year if not utilised
- To gain tax free income

- Due to Barbara being fully retired in 2020/21 and not at SPA she will be a non tax payer
- Jim should claim the marriage allowance to obtain tax reducer of 10% of Barbara's unused personal allowance as a tax reducer

- FXD Corporate Bond Unit Trust should be transferred to Barbara in full
- She can utilise starting rate band from when her SPA starts

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CGT Process and Calculation….

- Salary = £21,850
- OEIC Gain 2019/20 = £10,000
- Gilt Gain 2019/20 = £11,000
- Unit Trust Loss 2019/20 = £5,000
- Furnished Holiday Let Gain 2019/20 = £20,000*
- Buy to Let Gain 2019/20 = £30,000
- Previous C/F Losses = £8,300
- Annual exemption is available

(Question, Plan, Knowledge, Application)

*ER Qualifying

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CGT – Using Exemption and Losses

Q	NQ	NQP
FHL £20,000	OEIC £10,000	BTL £30,000
		- £5,000
		- £12,000
		- £8,300
£20,000	+ £10,000	+ £4,700

- Unit Trust Loss 19/20 = £5,000
- Annual Exemption
- C/F Losses

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CGT – Applying the Tax

BRB £37,500

		Rate
NQP: £4,700	BTL	28%
NQ: £1,850	OEIC	20%
NQ: £8,150	OEIC	10%
Q: £20,000	FHL	10%
Taxable Income £9,350	£21,850 - £12,500	

Create your CGT Stack!

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CGT Calculation

Basic Rate Band Remaining (BRB)

- £37,500 - £9,350 = £28,150
- FHL Gain: £20,000 x 10% = **£2,000**
- £20,000 BRB used so £8,150 remaining for OEIC Gain
- So (£8,150 x 10%) + (£1,850 x 20%) = **£1,185**
- No BRB remaining so entire BTL gain taxed at higher rate
- £4,700 x 28% = **£1,316**
- **Total CGT = £4,501**

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Asher, aged 64, is married to Esther, aged 65. They have two children aged 34 and 32, neither of whom are financially dependent on them. Esther retired a couple of months ago and is now in receipt of a defined benefit pension income of £18,653 per annum. In addition to this, Esther will start to receive a State Pension of £9,500 per annum from May 2020. Asher is currently self-employed and would like to retire when he reaches his 65th birthday in June 2020. He recently received details of his retirement options at age 65 from a former employer's defined benefit pension scheme as shown in the table below:

Full immediate pension of	£6,520 per annum
or	
Pension Commencement Lump Sum	£30,688
Plus, a reduced pension of	£4,602 per annum
or	
Cash equivalent transfer value (CETV) of	£228,200

The only other pension that Asher has accrued is a forecasted State Pension of £8,200 which will become payable when he reaches State Pension age in June 2021. Asher and Esther estimate they will require a total joint annual net income of £35,000 in retirement. Their only other assets are a mortgage free main residence valued at £340,000, cash savings of £15,000 and a stocks and shares ISA portfolio in Asher's name valued at £62,000. Asher would like advice in respect of his former employer's defined benefit scheme. He is unsure whether he should take his benefits from the scheme or transfer to a personal arrangement in order to access his benefits flexibly. Asher has an adventurous attitude to investment risk whereas Esther is cautious.

List five potential benefits and five potential drawbacks of Asher transferring the value of his defined benefit pension into a personal pension plan to access benefits flexibly **(10 Marks)**

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Benefits….

- Can vary the income being withdrawn, as state pension will be available in the future
- Potential for investment growth, as funds will be invested post crystallisation
- PCLS is likely to be greater, as 25% of CETV greater than available from ceding scheme
- Death benefits will likely be higher and more flexible as lump sum available from DC and spouses pension likely to be limited to 50% of member benefit
- Death benefits will be tax-free if death is before age 75, whereas all DB ongoing income is taxed on recipient PAYE regardless of age of death

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Drawbacks….

- Loss of guaranteed pension/exposure to investment risk, as DB is protected at 90% of benefit via the PPF
- Loss of escalation in payment/inflation risk, as DB scheme has guaranteed escalation rates
- Longevity risk, if he were to live a long life then funds could run out
- Subject to Sequencing Risk, when taking income from a fund during a falling market
- Costs/charges/complexity, as there are no explicit charges within the DB arrangement

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Question: Factors to Consider (Death Benefits)

James, aged 64, is married to Penny, aged 62. James is in poor health with a family history of death occurring before reaching average life expectancy. Penny is in excellent health with a family history of longevity. The couple have a low to medium attitude to investment risk and two adult, non-dependant children. Penny's only pension is a small State pension payable when she reaches age 66.

James is a deferred member of his previous employer's defined benefit scheme. The scheme will pay him an income of £40,000 per annum when he reaches age 65. The scheme, which offers a 2/3rds dependant's pension and includes a 10 year guarantee, has confirmed that James can transfer his benefits to a contract offering flexible benefits if he wishes and has offered him a CETV of £1,400,000.

Based on the information available, outline the factors you would consider in respect of the **death benefits** available before advising James on whether he should take his benefits from the scheme or transfer them to a contract providing flexible benefits. **(14 marks)**

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Answer: Factors to Consider (Death Benefits) (1/2)

- Penny only has very limited pension benefits in her own name **(1)** and so will be reliant on James's pension in the event he pre-deceases her **(1)** which appears likely given that she is in excellent health with a family history of longevity **(1)** and he is in poor health with a family history of dying earlier than average life expectancy **(1)**
- The DB scheme will provide her with a secure index linked income **(1)** whereas if James transfers Penny will be exposed to investment risk **(1)**
- The payments from scheme pension cannot be altered once in payment / she will be able to alter the levels of income she receives if James has transferred **(1)**

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Answer: Factors to Consider (Death Benefits) (2/2)

- The scheme pension is unlikely to provide Penny with a lump sum option on death **(1)** unless the value of any remaining guarantee period is valued at less than £30,000 **(1)**
- If James transfers then Penny can choose how she takes the benefits **(1)**
- A dependant's scheme pension cannot be paid to the children **(1)** whereas if James transfers then remaining funds can be passed to them following Penny's death **(1)**
- The income from a dependant's scheme pension will be taxed as Penny's pension income via PAYE **(1)** no matter what age James dies at **(1)** but if he transfers it will be tax free if he dies before age 75 **(1)**
- May be assessed for IHT if death occurs within two years of transfer **(1)**

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Current Protection Regimes

Michael, age 62, has the following pension arrangements:

- Value of pension rights on 5th April 2016 was £1.18m
- He took FP16 at this time and this is still active
- Current Value of pension rights is £1.24m

Question

- Explain why you would advise Michael to elect for IP16 Now (6)

(Question, Plan, Knowledge, Application)

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Current Protection Regimes - Answer

- If he were to decide to accrue benefits again in the future
- Then his FP16 would fail / break / cancel
- Which means his LTA would revert to SLA / £1.055m
- If he elects for IP16 now
- His LTA would be £1.18m
- As this was his pension rights value on 5th April 2016
- There are no downsides to doing so as further accrual is accepted for IP16

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IHT: Practice Question 1

Gail, a divorcee, died 1 October 2019 leaving her estate to her son. Her estate consisted of:

- House: £800,000
- ISAs: £200,000
- UTs: £400,000
- EIS: £250,000 (purchased in 2010)
- SIPP: £1.1m
- Chattels: £500,000

She placed £150,000 into a discretionary trust in May 2010 and gifted £300,000 to her son in June 2014. These were the only gifts she made.

Calculate, **showing all your workings**, the IHT **liabilities** that arise as a result of her death, and state who is responsible for paying them. **(16 marks)**

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IHT: Practice Question 1 (Answer)

TAX ON GIFTS

- No tax on the CLT as older than 7 years **(1)**
- **PET:** Failed as less than 7 years ago
  - NRB for PET: £325,000 - (£150,000 - £6,000)**(1)** = £181,000 **(1)**
  - Tax payable: [(£300,000 - £6,000) **(1)** - £181,000] x 40% x 40% taper (**1**) = £18,080 **(1)**
  - Payable by her son as the recipient of the gift **(1)**

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IHT: Practice Question 1 (Answer)

NRBs AVAILABLE

- **Standard NRB:** £325,000 – (£300,000 - £6,000) = £31,000 **(1)**
- **RNRB:**
  - Estate value is calculated as: £800,000 house + £200,000 ISAs + £400,000 UTs + £250,000 EIS **(1)** + £500,000 Chattels = £2.15 million **(1)**
  - Tapered RNRB: £150,000 – [(£2.15 million - £2 million) / 2] = £75,000 **(1)**

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IHT: Practice Question 1 (Answer)

TAX PAYABLE ON THE ESTATE

- **Estate value:** £800,000 house + £200,000 ISAs + £400,000 UTs + £500,000 Chattels
- = £1.9 million **(1)**
- **Allowable reliefs and exemptions:** £31k NRB + £75k RNRB = £106,000 **(1)**
- **Tax payable:** (£1.9 million - £106,000) x 40% (**1**) = £717,600 **(1)**
- Payable by the executors of her estate **(1)**

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IHT Protection Planning

Rod gifted Jane £331,000 on 1st December 2019 and then gifted Freddy £100,000 on Christmas Eve 2019, he then died leaving the balance of his estate to his foster child, George, on 5th January 2020. The balance of Rod's estate was £800,000, which included his main residence which was a converted windmill. Rod made no other gifts.

Explain in detail the protection policies that with hindsight, would have been recommended to all the individuals concerned (15)

(Question, Plan, Knowledge, Application)

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Strategy….

- When Rod made first gift to Jane, PET of £325,000, to effectively gift his NRB
- LTA, 7 years, **£130,000** Sum Assured, Own Life, In Trust to Executor
- Rod had no NRB to offset against his gift to Freddy, which was 2nd
- Gift Intervivos, Rod Life Assured in trust to Freddy or LOA, **£40,000** SA, would taper down after 3 years if Rod had survived
- No annual exemptions can be used on the £100,000 PET as used on gift to Jane
- £800,000 left for George, if LTA completed as above then effective NRB in place, as George is foster child then RNRB available at £150,000 for 2019/20.
- So WOL for Rod, SA 40% of £325,000 = **£130,000** in trust to Executors, indexation applied as estate likely to increase over time
- Review WOL each tax year as RNRB increasing by £25,000 in following tax year so could effectively be reduced by £10,000 SA next tax year

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Nicola, aged 63, is married to Reg, aged 62. They are both in good health. The couple have two children; Abigail, aged 36, who is married with two children and Olivia, aged 32, who is unmarried. Nicola has run her own limited company for the last 20 years but now plans to retire and so is the process of selling her 100% shareholding. She has been informed by her accountant that the capital gain following the sale will be £800,000 and this will fully qualify for entrepreneur's relief. Nicola's income from the business in 2019/20 will be £38,350. Nicola and Reg, who both have a medium to high attitude to risk, have the following investment portfolio:

Owner	Asset	Current value	Income received in 2019/20
Joint	Current account	£20,000	n/a
Joint	Building society savings account	£70,000	£700
Joint	Blue chip share portfolio	£120,000	£7,200
Joint	FXD Corporate Bond Unit Trust	£125,000	£4,370
Nicola	Onshore investment bond	£160,000	n/a
Nicola	ISA – ABC UK Equity Growth Fund	£165,000	£1,750
Reg	SJP ISA – Balanced Portfolio	£127,000	£3,800

Explain in detail the factors you would take into account when deciding whether to recommend that Nicola invests some of the proceeds from the sale of the business into an Enterprise Investment Scheme (EIS). You are not required to make a recommendation in your answer (15 Marks)

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Strategy….

- The capital gains tax incurred on the sale of the business can be deferred providing reinvestment takes place within three years of the sale.
- If the EIS is held on Nicola's death, there will be no CGT to pay.
- BR will be retained as when the business was sold it qualified for BR providing proceeds are reinvested within three years.
- This will reduce their estate for IHT purposes.
- The investment into the EIS is a tax reducer at 30% for Income Tax purposes.
- Nicola is unlikely to benefit fully from this as her Income Tax liability is too low for 2019/20, however she could carry back part of the investment to 2018/19 to increase the benefit achieved.
- An EIS is a high-risk investment that does not typically produce an income but is in line with Nicola's ATR.
- In addition, she has experience of investing and they have sufficient other means of producing an income so have sufficient CFL.

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