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Flight plan for success

Pension Income and IHT





Flight plan for success

Pension Income and IHT



This content is based on our understanding of current taxation, legislation and HM Revenue & Customs practice all of which are liable to change without notice. The impact of any taxation (and any tax reliefs) depends on individual circumstances.

Where content includes case studies or examples these are for illustration purposes and are not recommending a specific course of action.

Past performance is not a reliable indicator of future performance. The value of an investment can go down as well as up and your client may get back less than they've paid in.

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“Your pensions tax is gut-wrenchingly unjust”

‘You’ve stolen my happy retirement’: the letter shaming Rachel Reeves



“Your pensions tax is gut-wrenchingly unjust”

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What have been your clients' responses to the proposals?

① Start presenting to display the poll results on this slide.

Learning objectives

By the end of this session, you'll be able to:

1.

Describe the proposed changes to pensions and IHT legislation.

2.

Identify and examine how this will impact particular clients.

3.

Define which clients need to take action in the short/medium terms and the impact this will have on your advice process.

5.52 Inheritance tax: unused pension funds and death benefits – The government will bring unused pension funds and death benefits payable from a pension into a person's estate for inheritance tax purposes **from 6 April 2027**. This will restore the principle that pensions should not be a vehicle for the accumulation of capital sums for the purposes of inheritance, as was the case prior to the 2015 pensions reforms.

IHT on Pensions/Destination 2027

Summary

We welcome views on this technical consultation on the processes required to implement changes to Inheritance Tax rules for pension funds and death benefits.

This consultation closes at
11:59pm on 22 January 2025

Consultation description

As announced at Autumn Budget 2024, from 6 April 2027 most unused pension funds and death benefits will be included within the value of a person's estate for Inheritance Tax purposes and pension scheme administrators will become liable for reporting and paying any Inheritance Tax due on pensions to HMRC.

This is a technical consultation on the processes required to implement these changes for UK-registered pension schemes. It is likely to be of interest to individuals, pension scheme administrators and other pensions professionals, tax and legal practitioners.

After the consultation, the government will publish a response document and carry out a technical consultation on draft legislation for these changes in 2025.

Current IHT on pension schemes

Power of Disposal
(with some
exceptions)

Within estate

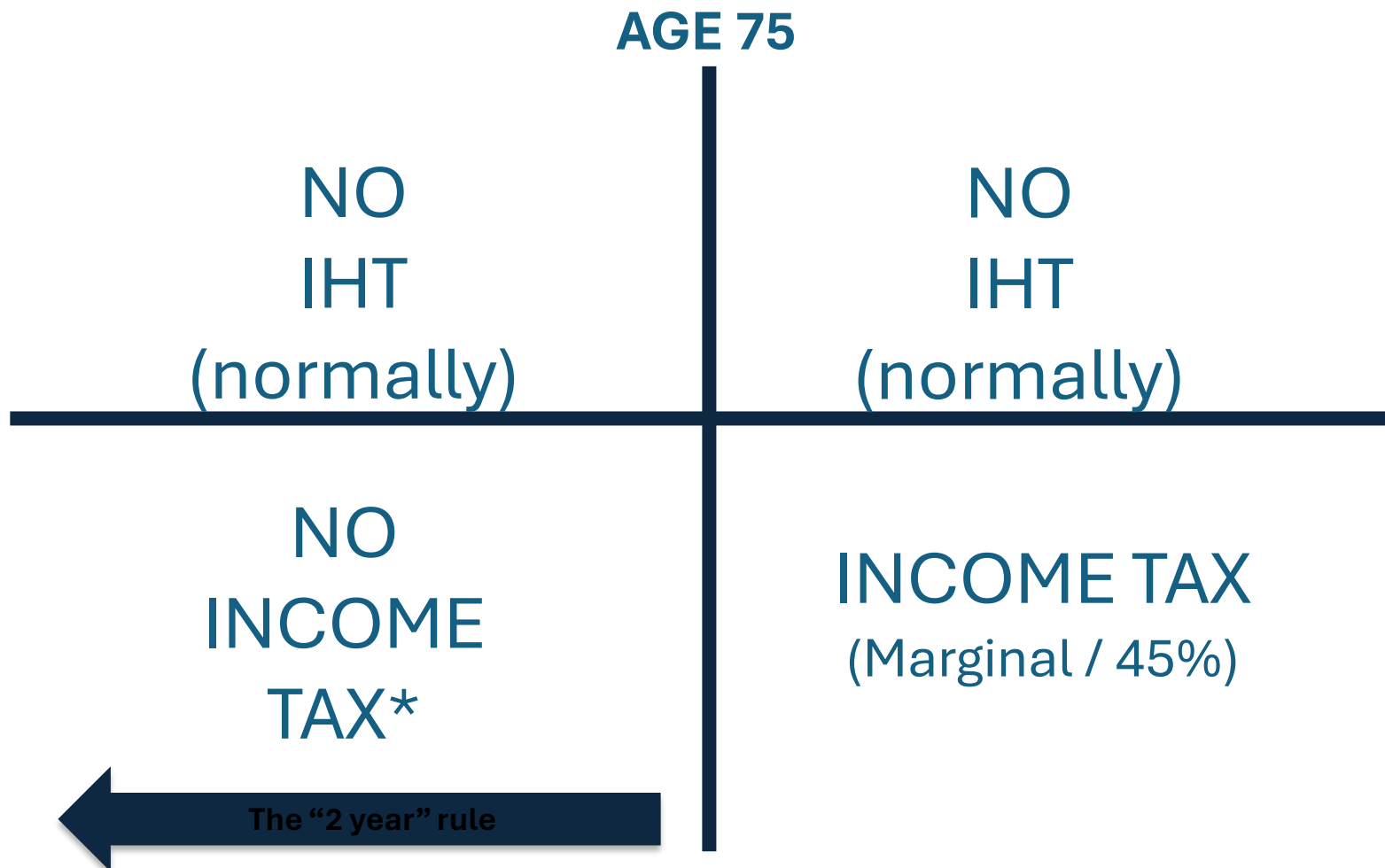
Estate entitled

Within estate

Discretionary
Disposal

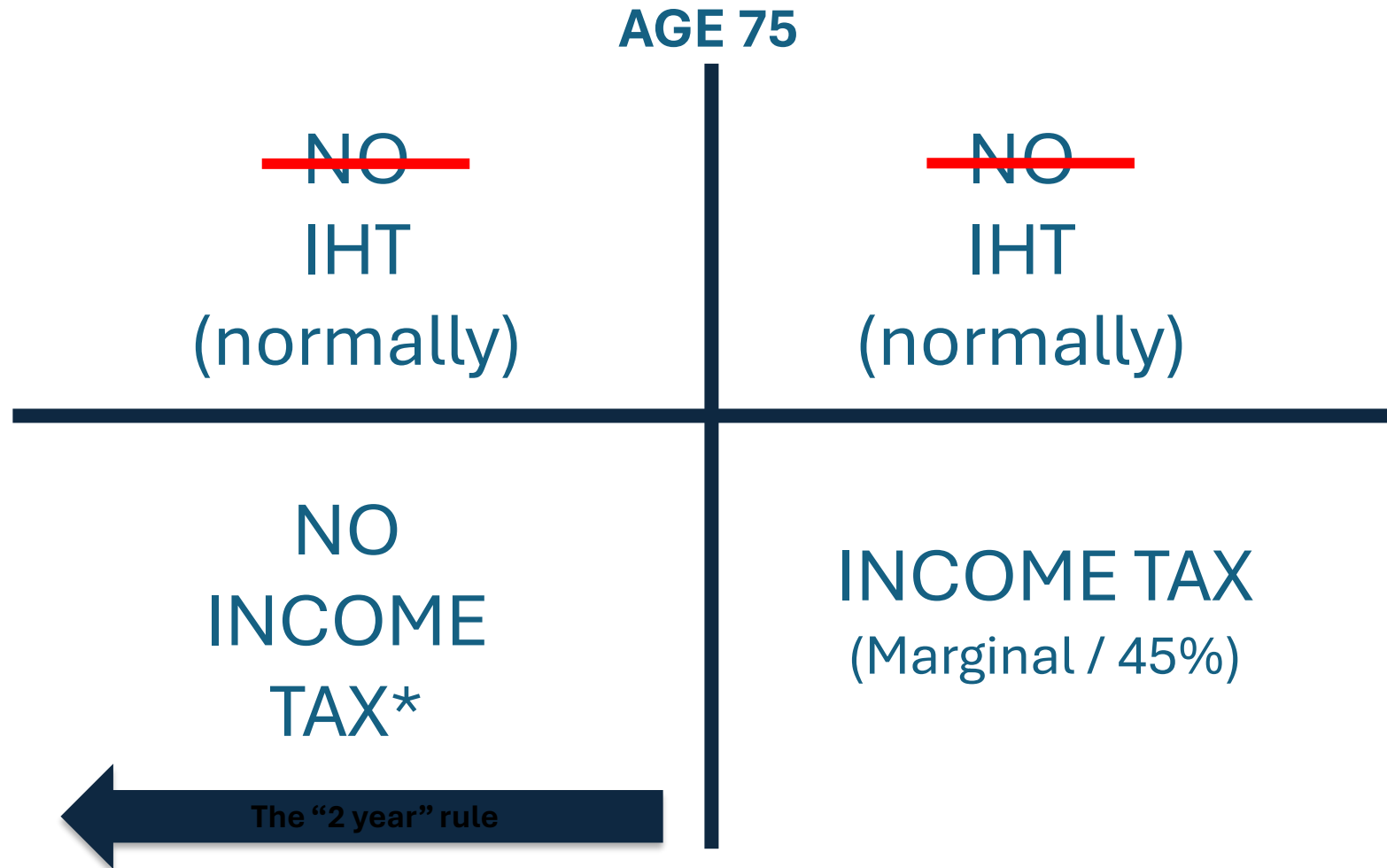
~~Outside estate~~
Within estate

Where we are until 2027



* DB income is taxable

Where we're going



* DB income is taxable

Both taxes will apply

Process/Runway

LPRs request values from pension schemes

Pension Scheme notifies LPRs of values

LPRs identify NRB for scheme with new HMRC tool

LPRs notify scheme of NRB available for pension

Scheme calculates IHT liability and pays HMRC

Balance distributed under current scheme and pension tax rules



DB and DC

EXEMPT

Charity Lump Sums

Dependants Scheme Pensions

NOT EXEMPT

ALL Dependent Benefits

ALL Nominee Benefits

ALL Successor Benefits



- **Emily 73**
- **Value of estate £800,000**
- **Pension fund value £700,000**

Case study



2025

Current

2027

Potential position

| | 2025 | 2027 |
|--------------------------------------|-----------------|--------------------------------|
| | Current | Potential position |
| Value of estate | £800,000 | £800,000 |
| Pension fund for IHT | £0 | £700,000 |
| Total liability | £800,000 | £1,500,000 |
| Nil Rate Band | (£325,000) | (£325,000) |
| Total value for IHT | £475,000 | £1,175,000 |
| IHT @ 40% | £190,000 | £470,000 |
| IHT paid by pension scheme | N/A | 470,000*7/15 = £219,333 |
| IHT paid by personal representatives | £190,000 | 470,000*8/15 = £250,667 |

Why do I have my pension?

Plan was always to spend on retirement then business as usual!



INCOME
SUSTAINABILITY



CASH FLOW
MODELLING



THEMATIC
REVIEW



CRP



INVESTMENT
SOLUTIONS

Are pensions still the best vehicle to fund retirement?

Tax relief at highest marginal rate



Tax free growth



Tax free cash



IHT free to spouse



Case Study Pre Retirement – distribution of assets in the event of death prior to retirement

- Stuart age 50
- Pension pot - £1.5m
- Spouse
- Adult child from previous relationship
- Planning to split pension 50%/50%



Case Study Pre Retirement – distribution of assets in the event of death prior to retirement

Pre April 2027

- Prior to budget no IHT considerations both receive same amount - £750k

Post April 2027

- Spouse will receive £750k
- Child assuming nil rate band used will receive
- $£750k - £325k = £425k$
- $£425k * 40\% = £170,000$
- Adult child now receives £580k

Life expectancy

78.6



82.6



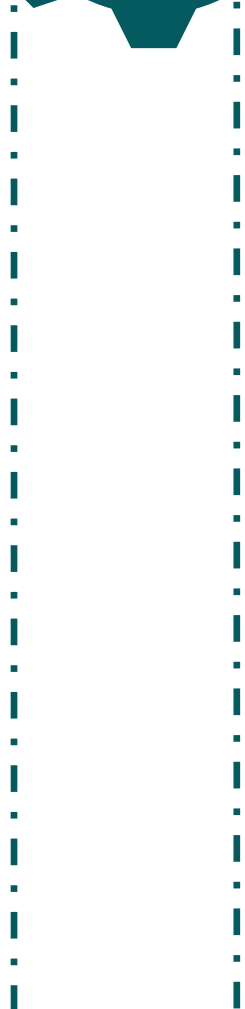
What we don't know



“Planning is always conducted in an uncertain world”



What we
do know

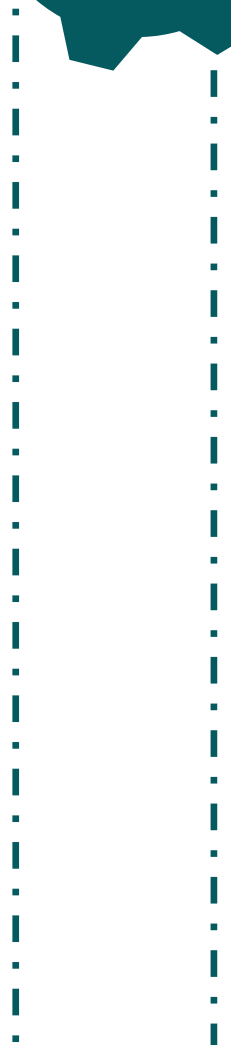


Clients who haven't taken tax free cash and are 75 or above



Conversation points

- What are client objectives?
- Consider taking tax free cash
- Gifting?
- Beneficiary drawdown pots?



Clients who haven't taken tax free cash and are 75 or above



Clients who are currently funding pensions to pass on



Conversation points

- Do you continue?
- Fund pensions for others?



Clients who haven't taken tax free cash and are 75 or above



Clients who are currently funding pensions to pass on



Clients who are drawing income from other assets currently and leaving pension



Conversation points

- Reconsider using pension income first?
- No one size fits all
- Cash flow modelling imperative



Clients who haven't taken tax free cash and are 75 or above

Clients who are currently funding pensions to pass on

Clients who are drawing income from other assets currently and leaving pension

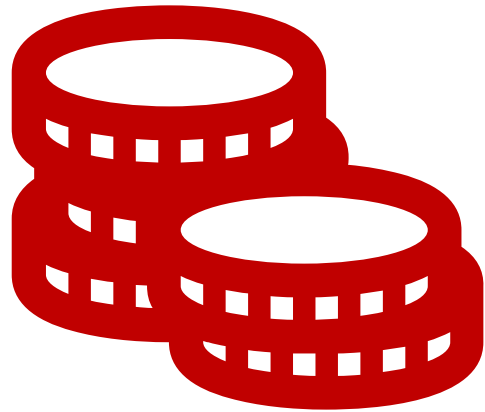
Clients who have complicated family situations



Conversation points

- What is the clients' main concern?
- No one size fits all
- Spousal Bypass trusts back in vogue?



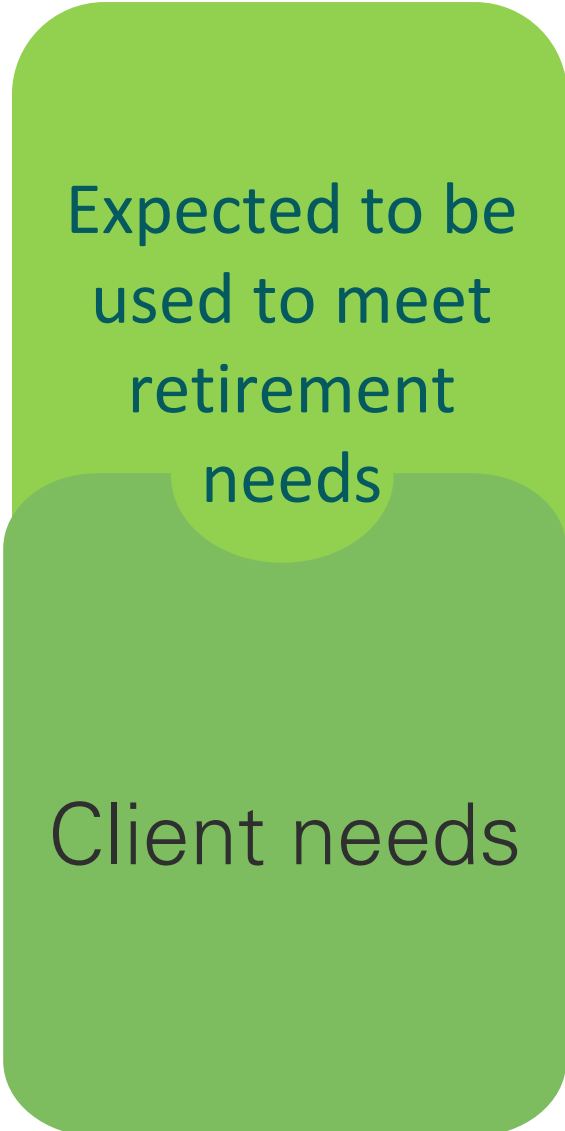


Red money

Identifying red money



Identifying red money



Expected to be used to meet retirement needs

Client needs



Client peace of mind



Client legacy

Identifying red money

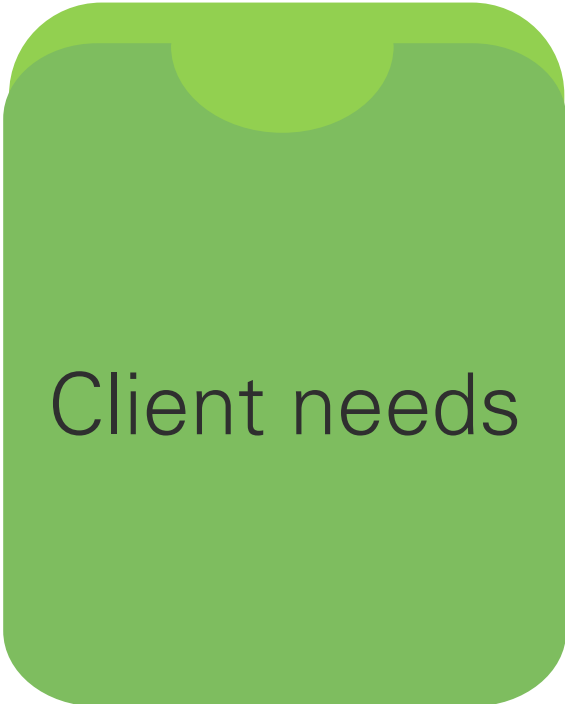
Client needs

May be required to meet retirement needs

Client peace of mind

Client legacy

Identifying red money



Finding the correct flight path

Sustainability
of income to
last the client
until death

vs

Surplus funds
for loved
ones



Cash flow modelling

- Help clients understand the impact of financial circumstances and how this could affect their income
- Provide information to help them understand the recommended product
- Highlight the potential risks
- Help make an informed financial decision

RETIREMENT INCOME ADVICE ASSESSMENT TOOL

| | | | | |
|--|--|--|--|--|
| Name of NMPI or non-standard investment. | | | | |
| Name of provider | | | | |
| Additional comments on NMPIs | | | | |
| Page Ref: | | | | |

| Withdrawal details | Product 1 | Product 2 | Product 3 | Product 4 |
|--|------------------|------------------|------------------|------------------|
| Withdrawal type | | | | |
| Withdrawal strategy | | | | |
| Additional comments on withdrawal strategy | | | | |
| Withdrawal frequency | | | | |
| <i>Lump sum withdrawals</i> | | | | |
| Pension - PCLS (£) | | | | |
| Pension - Taxable income (gross) (£) | | | | |
| Non pension withdrawal (gross) (£) | | | | |
| <i>Ongoing withdrawals (annualised)</i> | | | | |
| Pension - PCLS (£) | | | | |
| Pension - Taxable income (gross) (£) | | | | |
| Non pension withdrawal (gross) (£) | | | | |
| Additional comments on withdrawals | | | | |
| Page Ref: | | | | |

RIAAT – withdrawal strategies

Withdrawal strategy

3.24 Various withdrawal strategies may be employed by a firm to assist a client to achieve their objectives for their retirement savings. Below we list some examples of common withdrawal strategies we have seen used in relation to flexible benefits. This list is not exhaustive and a firm may use multiple withdrawal strategies.

Within the RIAAT there are seven identified withdrawal strategies

(a) A “sustainable withdrawal rate”



(b) A “natural income” or “natural yield” strategy



(c) A “multiple pots” strategy



(d) “Bridging to other income”



(e) A “withdrawal minimisation”

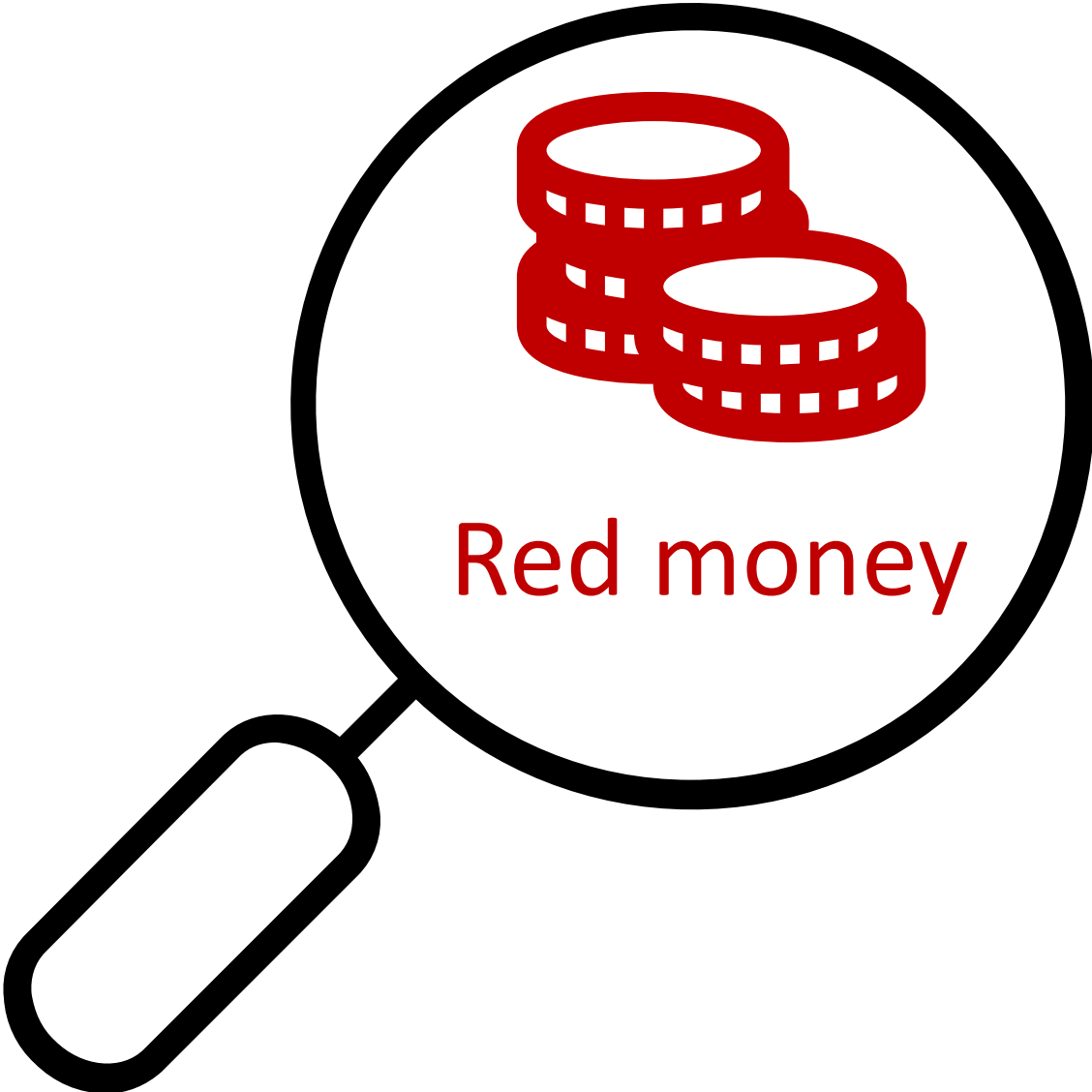


(f) A “fixed/short-term annuities”



(g) An “ad hoc withdrawals only”





What to do if you
have an IHT
surplus?



or it Accept it Insure it Plan for it Accept it In

What to do if you
have an IHT
surplus?



or it **Accept it** Insure it Plan for it Accept it In

What to do if you
have an IHT
surplus?



pt it Insure it Plan for it Accept it Insure it Pla

What to do if you
have an IHT
surplus?



Plan for it Accept it Insure it Plan for it

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Which option do you think most clients will choose?

① Start presenting to display the poll results on this slide.

Head or heart?



Head or heart?

- IQ v EQ
- Is it the number or the emotional effect?
- What is the client's driver?
- Is it looking after themselves and their retirement needs (don't care what happens I won't be here).
- Or I want to ensure my money goes exactly where I want it to, even if that means more tax.
- Or I just want to pay the least amount of tax.



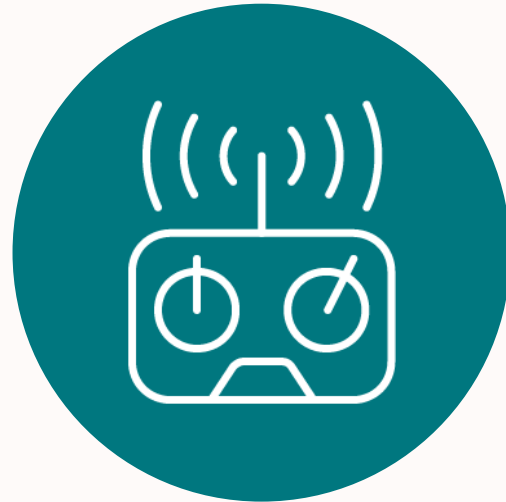
IHT planning hasn't changed



Access

Your client

Their beneficiaries



Control

Owning directly

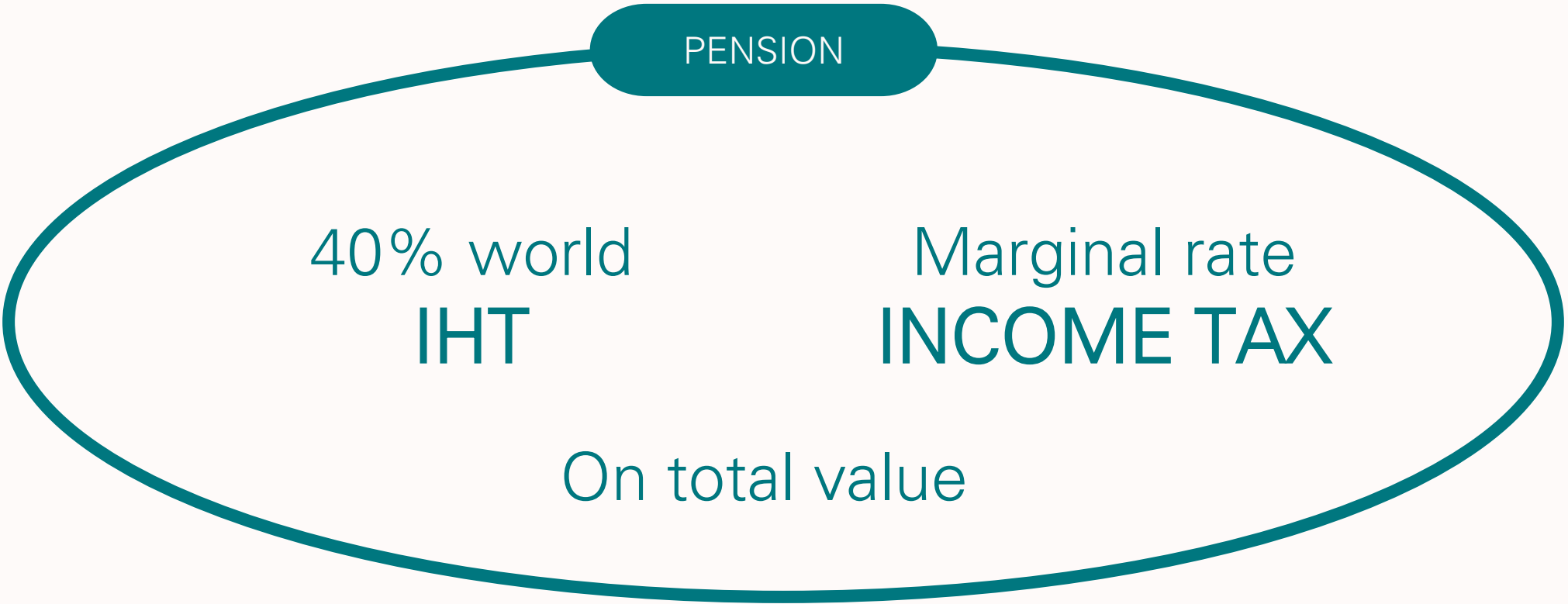
"Trusteeship"



Tax

It follows!

Should I stay or should I go?



IHT
0% or 6% or 40% world

Income / Gains
0% to 45%
growth & income only

| Scenario | 1 | 2 | 3 | 4 | 5 | 6 | 7 |
|---------------|-------------------------|--------------------------|------------|----------|-------------|-----------------|-----------------------------------|
| | In pension death pre 75 | In pension death post 75 | Loan trust | Gift | Exempt Gift | Business relief | In pension death post 75 (no IHT) |
| Growth | 5% | 5% | 5% | 5% | 5% | 3% | 5% |
| Pension value | £100,000 | £100,000 | £100,000 | £100,000 | £100,000 | £100,000 | £100,000 |

| | | | | | | | | |
|--|-----|----------|----------|----------|----------|----------|----------|----------|
| IHT (assume no NRB) | 40% | £0 | £0 | £40,000 | £40,000 | £0 | £42,436 | £0 |
| Income tax | 20% | £0 | £22,050 | £2,050 | £2,050 | £2,050 | £0 | £22,050 |
| Net legacy | | £110,250 | £88,200 | £68,200 | £68,200 | £108,200 | £63,654 | £88,200 |
| Death after April 2027 (just over 2 years) | | | | | | | | |
| Gross value | | £110,250 | £110,250 | £110,250 | £110,250 | £110,250 | £106,090 | £110,250 |
| IHT (assume no NRB) | 40% | £44,100 | £44,100 | £40,000 | £40,000 | £0 | £0 | £0 |
| Income tax | 20% | £0 | £13,230 | £2,050 | £2,050 | £2,050 | £0 | £22,050 |
| Net legacy | | £66,150 | £52,920 | £68,200 | £68,200 | £108,200 | £106,090 | £88,200 |
| Death after April 2032 (just over 7 years) | | | | | | | | |
| Gross value | | £140,710 | £140,710 | £140,710 | £140,710 | £140,710 | £122,987 | £140,710 |
| IHT (assume no NRB) | 40% | £56,284 | £56,284 | £40,000 | £0 | £0 | £0 | £0 |
| Income tax | 20% | £0 | £16,885 | £8,142 | £8,142 | £8,142 | £0 | £28,142 |
| Net legacy | | £84,426 | £67,541 | £92,568 | £132,568 | £132,568 | £122,987 | £112,568 |

| Scenario | 1 | 2 | 3 | 4 | 5 | 6 | 7 |
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Death before April 2027 (just under 2 years)

| | | | | | | | | |
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| Net legacy | | £84,426 | £67,541 | £92,568 | £132,568 | £132,568 | £122,987 | £112,568 |

Planning with pensions



Draw more income than I need

Consolidation – make life easier for family – beware of possible de-minimis

Gifting

Review nomination forms – discretion to direction if allowed

Pension and ISA contributions for grandchildren

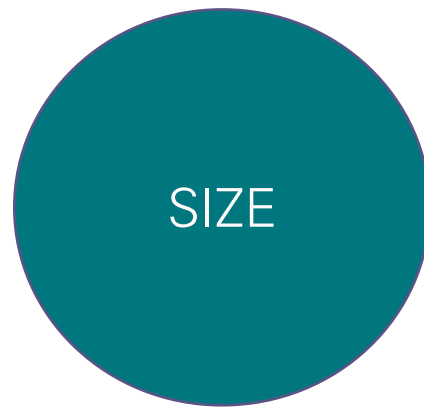
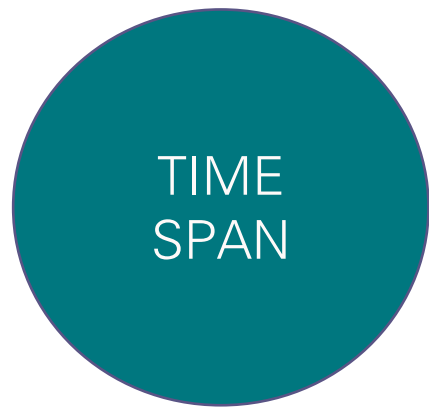
Review DIS v group life/relevant life policies

Using exemptions and NEOOI

Liquidity of assets – SIPP/SSAS with property

Normal Expenditure Out of Income

5 things you need to know



Drawdown Income, PCLS and UFPLS are income



RETIREMENT

PRIORITY

- Identify red money – segmentation
- Clients post 75 TFC
- Client who may need expression of wish changed

GENERAL BOARDING

- Clients looking to gift money
- Clients topping up red money
- Clients with Red money but feel “they might need it”

SPECIAL ASSISTANCE

- Consolidation to make life easier for family
- Beware of possible de-minimis
- Annuities – rules still unclear

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What will you be advising clients to do with their red money?

① Start presenting to display the poll results on this slide.

Learning outcomes

By the end of this session, you'll be able to:

1.

Describe the proposed changes to pensions and IHT legislation.

2.

Identify and examine how this will impact particular clients.

3.

Define which clients need to take action in the short/medium terms and the impact this will have on your advice process.

Red money – destination unknown



EGRs – expectation and reality

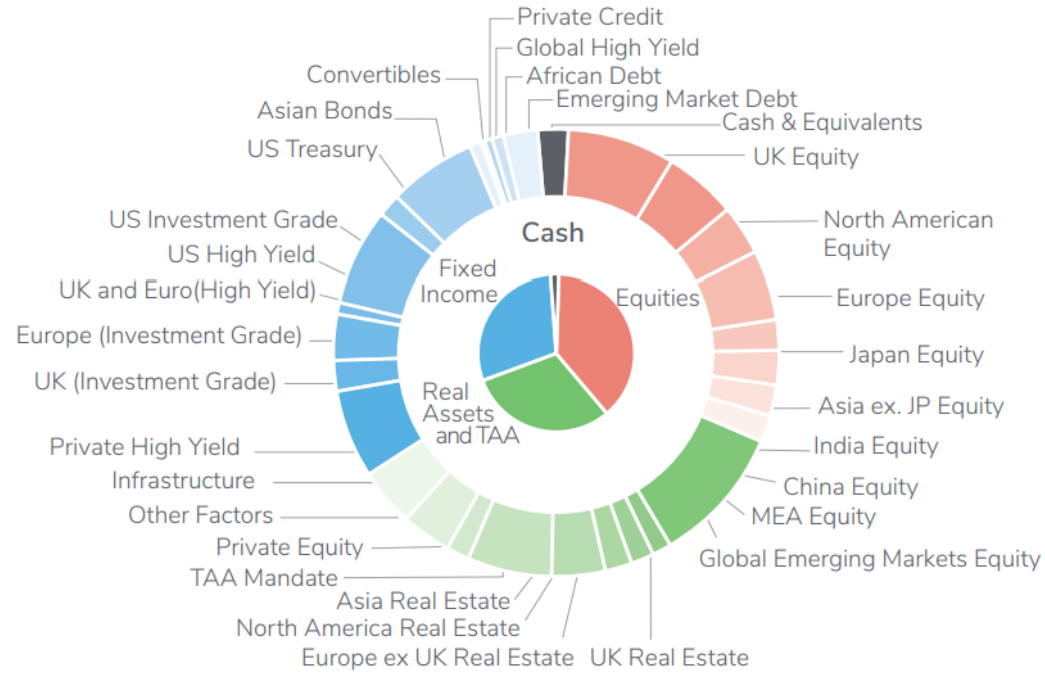
| Investment date | PruFund Growth EGR at outset | PruFund Return after 10 years | ABI Mixed 20-60% Shares return after 10 years |
|-----------------|------------------------------|-------------------------------|---|
| 25/11/2004 | 6.60% | 6.64% | 4.33% |
| 25/11/2005 | 6.60% | 6.21% | 3.36% |
| 25/11/2006 | 6.85% | 5.74% | 3.26% |
| 25/11/2007 | 6.85% | 5.56% | 4.00% |
| 25/11/2008 | 6.85% | 7.64% | 5.85% |
| 25/11/2009 | 6.60% | 7.20% | 4.58% |
| 25/11/2010 | 6.60% | 6.21% | 3.92% |
| 25/11/2011 | 6.60% | 6.64% | 4.82% |
| 25/11/2012 | 6.20% | 6.61% | 2.96% |
| 25/11/2013 | 6.20% | 6.03% | 2.17% |
| 25/11/2014 | 6.00% | 6.13% | 2.58% |

Figures are for PruFund Growth Fund held within PruFund Investment Plan. The PruFund figures include any additional investment expenses, but not any fund management, product or advice charges, so the amount an investor would get back would be less than shown here. Some, if not all, of the funds comprising the ABI sector average are net of fund charges. Past performance is not a reliable indicator of future performance. The value of an investment can go down as well as up. Source: Prudential and FE Analytics

PruFund vs peer

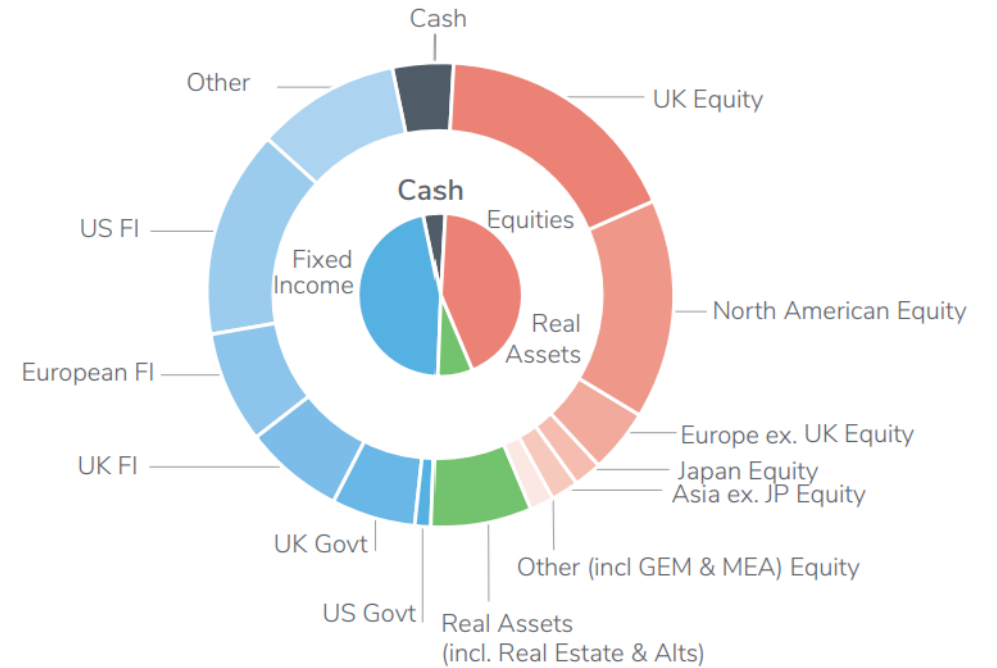
PruFund Growth

Source: Prudential Actuarial.
Date: at end September 2024.

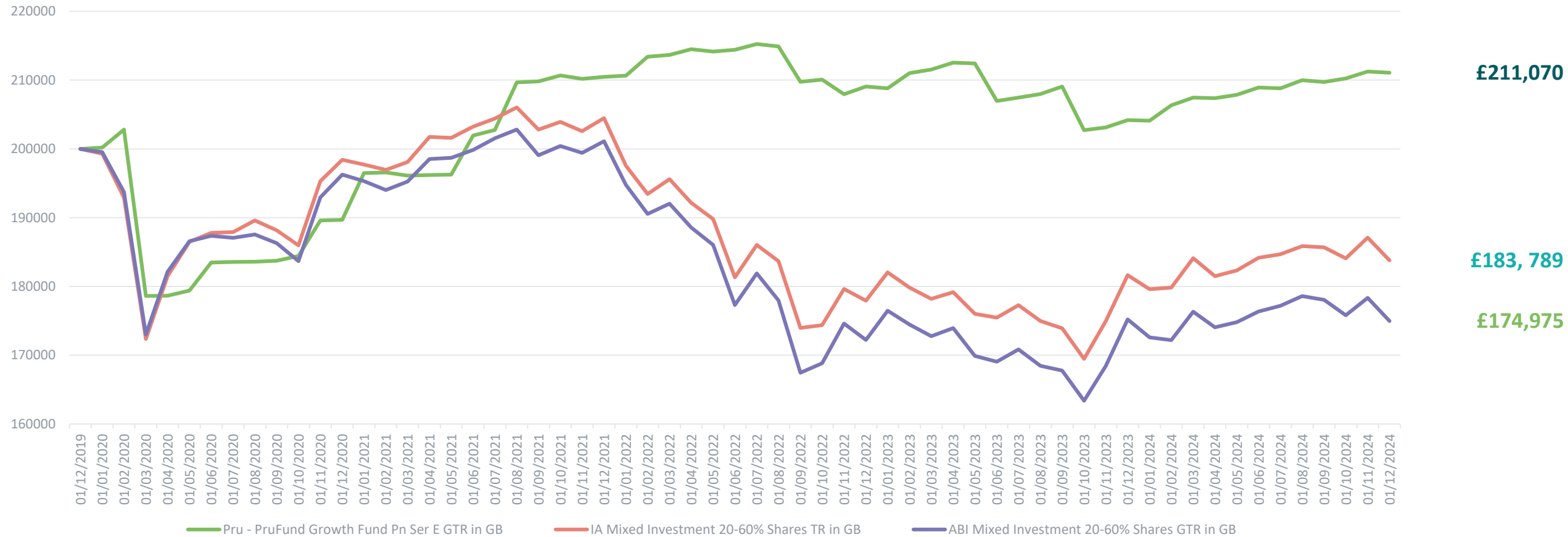


Average Peer Allocation

Source: M&G Treasury & Investment Office.
Date: at end September 2024.

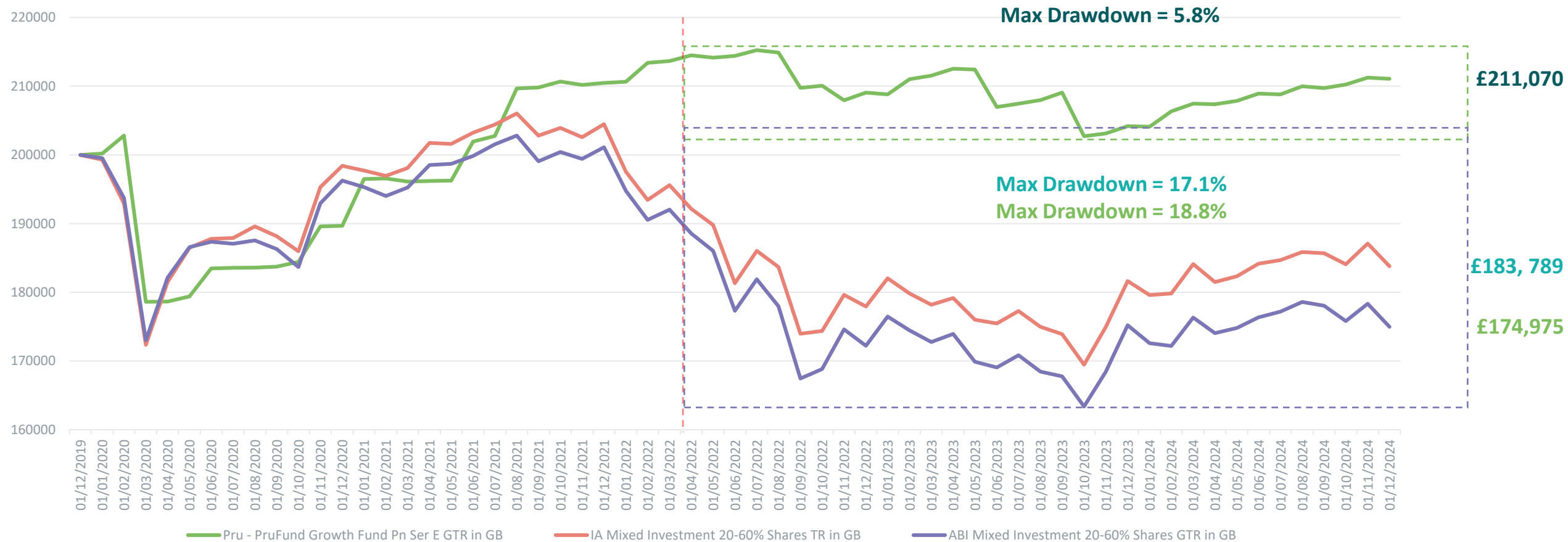


Performance of PruFund Growth with 4% withdrawals – 5 yrs



Figures are for PruFund Growth Pn Ser E and are for the period from 31 Dec 2019 to 31 Dec 2024. The initial investment is £200,000 and regular withdrawals of £666.67 are taken at the end of each month. The PruFund figures include any additional investment expenses, but not any product or advice charges, so the amount an investor would get back would be less than shown here. Some, if not all, of the funds comprising the IA and ABI sector averages are net of fund charges. Past performance is not a reliable indicator of future performance. **The value of an investment can go down as well as up. Your clients may get back less than they have paid in.** Source: FE Analytics

Performance of PruFund Growth with 4% withdrawals – 5 yrs



Figures are for PruFund Growth Pn Ser E and are for the period from 31 Dec 2019 to 31 Dec 2024. The initial investment is £200,000 and regular withdrawals of £666.67 are taken at the end of each month. The PruFund figures include any additional investment expenses, but not any product or advice charges, so the amount an investor would get back would be less than shown here. Some, if not all, of the funds comprising the IA and ABI sector averages are net of fund charges. Past performance is not a reliable indicator of future performance. **The value of an investment can go down as well as up. Your clients may get back less than they have paid in.** Source: FE Analytics

Historic maximum withdrawal rate without erosion of capital

Table shows maximum withdrawal rate, as % of initial investment, that can be taken without loss of initial investment at end of time period indicated

| | Start 31/12/2014 (10 years) | Start 31/12/2015 (9 years) | Start 31/12/2016 (8 years) | Start 31/12/2017 (7 years) | Start 31/12/2018 (6 years) | Start 31/12/2019 (5 years) |
|---|--------------------------------|-------------------------------|-------------------------------|-------------------------------|-------------------------------|-------------------------------|
| IA Mixed Investment 0-35% Shares Sector | 2.3% | 2.6% | 1.8% | 1.4% | 2.2% | 1.0% |
| IA Mixed Investment 20-60% Shares Sector | 3.7% | 4.0% | 3.2% | 2.6% | 4.0% | 2.4% |
| IA Mixed Investment 40-85% Shares Sector | 5.4% | 5.8% | 4.9% | 4.1% | 6.1% | 4.1% |
| PruFund Cautious Pn Ser A | 4.2% | 3.9% | 4.3% | 3.8% | 4.1% | 4.0% |
| PruFund Growth Pn Ser A | 6.1% | 5.6% | 5.6% | 5.2% | 5.1% | 5.1% |

Figures for PruFund Growth Pension and PruFund Cautious Pension are gross of tax. Figures are over the time period shown to end of December 2024. Initial investment of £100,000 and withdrawals taken at the end of the month. Past performance is not a reliable indicator of future performance. Both PruFund Growth Pension and PruFund Cautious Pension include a representative annual charge of 0.65% and any additional investment expenses, but not any product or advice charges, so the amount an investor would get back would be less than shown here, Some, if not all, of the funds comprising the IA sector averages are net of fund charges. This example represents a typical situation. It is not related to any particular individual and does not recommend that course of action. Source: FE Analytic.

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Historic maximum withdrawal rate without erosion of capital

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| PruFund Growth Pn Ser A | 6.1% | 5.6% | 5.6% | 5.2% | 5.1% | 5.1% |
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The value of an investment can go down as well as up. Your clients may get back less than they have paid in.



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