CII NOTTINGHAM SEPTEMBER 2017

BARRY FOSTER FPFS IMC TEP
TECHNICAL MANAGER

A WEALTH *of* DIFFERENCE

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LEARNING OBJECTIVES

By the end of the session delegates will be able to;

- Appreciate some of the high level differences between certain investment tax wrappers including:
  - The internal taxation
  - The availability to clients of certain income tax allowances
  - The tax planning opportunities presented by a portfolio of multiple tax wrappers within a client portfolio.
- Be able to discuss and explain this subject with a client in a clear and concise way
- Apply this knowledge to appropriate, individual, client scenarios.

AGENDA

- Tax wrappers – a high level comparison
- LISA Vs Pension
- Overseas pension schemes
- 2017/18 income tax bands
- Chargeable gains and the income tax allowances
- Offshore bonds and retirement planning
- The power of numbers

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TAX WRAPPERS

A HIGH LEVEL COMPARISON

TAX WRAPPER – TAXATION WITHIN THE TAX WRAPPER (2016/17)

	PENSION	ISA	OEIC	OFFSHORE BOND	ONSHORE BOND
TAX RELIEF ON CONTRIBUTIONS	Y	N Y?*	N	N	N
INTEREST	0%	0%	20%** (0%)	0%	20%
DIVIDENDS	0%	0%	0%	0%	0%
GROWTH	0%	0%	0%	0%	20%***

* LISA – bonus
**Interest may still be received net of corporation tax
*** Corporation tax after indexation allowance

THE TAX “Tea Urn?”

TAX ALLOWANCES POTENTIALLY AVAILABLE

Pension
- PCLS
- Personal allowance

ISA
- Tax free income and gains

Collectives
- Personal allowance
- Starting rate band for savings
- Personal savings allowance
- Dividend allowance
- CGT annual exemption

Onshore Bond
- Top slicing
- Tax credit for 20% tax paid within fund

Offshore Bond
- Top slicing
- Personal allowance
- Starting rate band for savings
- Personal savings allowance

THE TAX “Tea Urn?”

TAX ALLOWANCES POTENTIALLY AVAILABLE

IHT ESTATE	out	in *except AIM	in	in	in
	Pension	**ISA**	**Collectives**	**Onshore Bond**	**Offshore Bond**
	PCLS Personal allowance	Tax free income and gains	Personal allowance Starting rate band for savings Personal savings allowance Dividend allowance CGT annual exemption	Top slicing Tax credit for 20% tax paid within fund	Top slicing Personal allowance Starting rate band for savings Personal savings allowance

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LISA VERSUS PENSION

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LISA QUALIFICATION RULES

- Available from 6 April 2017
- Entry window age 18 - 40
- Up to £4,000 per annum
- Bonus of 25% paid at end of year i.e. £5,000 invested
- Paid until age 50
- If funds withdrawn before age 60 for any other reason than first property purchase government bonus plus growth clawed back.
- Maximum of £32,000 paid by government (plus growth!)

PROBLEMS, PROBLEMS!

Lifetime Isa take-up questioned as two-thirds in dark over availability

Is the industry "deliberately ignoring" the Lifetime ISA?

The Lifetime Isa: Free money - or just too complicated?

The Osborne hangover: Govt gets desperate on Lifetime Isas

LISA – 2017/18 UPDATE

- Secretary to the Treasury Jane Ellison confirmed, in a debate on the Savings (government contributions) Bill on 12th December 2016, that **the early withdrawal charge would not apply in 2017/18.**

- This is because the government bonus in respect of 2017/18 will not be paid until the end of the tax year and the charge relates, in part the withdrawal of the Government bonus.*

The 25% Government charge on unauthorised withdrawals from the lifetime ISA recoups the Government bonus and applies a small additional charge. This is fair as it reflects the long-term nature of the product and ensures that individuals save into it for the intended purposes, protecting Government funds and taxpayers' money. However, in 2017-18 only, the bonus will not be paid monthly, as it will be from April 2018 on, but will be paid as an annual bonus at year-end. This could create a difficult case where people face a 25% Government charge up to 12 months before they receive the bonus. We have listened to representations on this point, and so, to improve the product for consumers, I can confirm that there will be no Government charges in 2017-18.

If people want to withdraw from their lifetime ISA in 2017-18, they must close their account, and there will be no Government charge to do so. No bonuses will be paid on such closed accounts.

***in future tax years the bonus will be applied monthly**

Source: https://hansard.parliament.uk/Commons/2016-12-12/debates/B79CDD02-91CF-4BA7-BC33-A2EFC2DEAD3E/Savings(GovernmentContributions)Bill

COMPARISON OF SAVING INTO AND DRAWING BENEFITS FROM PENSION/LISA/ISA

£100 net contribution/subscription assuming no growth…

	Pension BRT relief	Pension HRT relief	Pension ART relief	LISA	LISA (early access)	ISA
Fund	**£125**	**£167**	**£182**	**£125**	**£125**	**£100**
BRT	**£106**	£142	£155	**£125**	£93.75*	£100
HRT	**£87**	**£117**	£128	**£125**	£93.75*	£100
ART	**£83**	**£111**	**£121**	**£125**	£93.75*	£100

*Reflects repayment of government bonus and charge for early access

Comparison assumes no investment growth for ease of comparison and assumes pension funds are drawn 25% tax free and 75% taxable at Basic, Higher and Additional rate tax (BRT / HRT / ART)

Note, LISA government bonus is allocated at the end of the tax year as compared with pension tax relief at source or higher/additional pension tax relief via self-assessment.

PENSION V ISA ON DEATH PRIOR TO AGE 75

BASIC RATE TAXPAYER

Contribution	Pension	ISA (not AIM)	LISA
£80 net	£100	£80	£100
Net benefit on death if estate not liable to IHT	£100	£80	£100
Net benefit on death if estate is liable to IHT	£100	£48	£60

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PENSION V ISA ON DEATH PRIOR TO AGE 75

HIGHER RATE TAXPAYER

Contribution	Pension	ISA (Not AIM)	LISA
£60 net (effective net cost)	£100	£60	£75
Net benefit on death if estate not liable to IHT	£100	£60	£75
Net benefit on death if estate is liable to IHT	£100	£36	£45

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OVERSEAS PENSION SCHEMES

QROPS & QNUPS

TWO OF THE CHOICES…

Qualifying Recognised Overseas Pension Scheme (QROPS)

Advantages for those that have been non UK resident for five/ten* complete tax years, **QROPS jurisdiction allowing!**

- Pension income paid without deduction of UK tax
- No tax deducted on death – crystallised or not
- 30% of the fund can be paid as PCLS
- Pension paid in appropriate currency
- Member payment charges no longer apply.

What about QROPs for UK residents?

Qualifying Non UK Pension Scheme (QNUPS)

- Expatriates saving for their retirement who may wish to return to the UK in the future
- High net worth UK residents or domiciled individuals who have paid their maximum UK pension contributions OR reached the maximum fund
- Individuals transferring from overseas pensions or QROPs
- Require another route to "top up" their benefits.
- Up to 30% tax free lump sum

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*Five years in respect of pre 6th April 2017 transfers

QROPS FOR UK RESIDENTS

Until the member has been non resident for more than ten* complete tax years, there is little difference between a UK registered scheme and a QROPS for a UK resident although:

- A transfer from a UK registered scheme to QROPS is BCE 8
- All growth from that point should not be assessed against the Lifetime Allowance
- This provides an opportunity to limit exposure to the Lifetime Allowance.

*Five years in respect of pre 6th April 2017 transfers

QUALIFYING NON-UK PENSION SCHEMES (QNUPS)

- Before A-Day certain non-UK pension schemes were protected from UK inheritance tax
- A-Day regulations omitted this exemption and meant that UK pension funds would be liable to IHT when transferred to QROPS
- The Inheritance Tax Regulations 2010, which came into force on 15th February 2010 solved this problem and also created QNUPS
- **QNUPs must broadly satisfy the same conditions as a ROPS.**

Source: http://www.legislation.gov.uk/uksi/2010/51/pdfs/uksi_20100051_en.pdf

QNUPS

BENEFITS

- Ability to take a lump sum of up to 30% (25% for UK residents)
- If income subject to UK tax, 100% taxable from 6 April 2017
- No requirement to purchase an annuity, although might have to take benefits at 75 e.g. Guernsey rules
- 100% return of fund on death for both crystallised and uncrystallised funds
- IHT not normally charged on death.

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2017 BUDGET UPDATE

Finance Bill 2017 includes new QROPS legislation:

- Increased reporting obligations on UK schemes transferring to QROPS
- Increased reporting requirements imposed on QROPS
- HMRC will retain rights to apply "member payment charges"

- **A 25% transfer charge may be applied on transfer from a UK registered scheme to a QROPS if certain conditions are not met;**

  - Member is transferring pension to a QROPS that is based in the same jurisdiction as the member
  - Both the member and the QROPS are in the EEA
  - Other criteria relating to occupation type schemes.

- The transfer charge can be reviewed if the member moves within 5 complete tax years of the date of transfer

- i.e. if an EEA resident moves away from the EEA within 5 years of the transfer from the UK scheme, the transfer charge can still be applied. If a non EEA resident moves into the EEA within 5 years of the transfer from the UK scheme, the transfer charge can be reclaimed from HMRC).

OVERSEAS PENSIONS

Overseas pensions offer planning opportunities for;

- Non-UK resident clients
- UK resident clients intending to become non-resident
- UK resident clients with concerns about their current pension arrangements.

QROPS

Clients wishing to transfer UK registered scheme funds so as,

- Access benefits abroad without deduction of UK tax at source
- Access benefits in different currencies
- To limit their exposure to the Lifetime Allowance.

QNUPS

- Clients affected by annual & lifetime Allowance restrictions
- Wishing to enhance their retirement provision in an IHT efficient way.

OVERSEAS PENSIONS

SUMMARY

The legislation is:

- Complicated and is a specialist area of advice,
- Has been subject to legislative change but…

Is it a suitable option for some clients and possibly a gap in your service offering?

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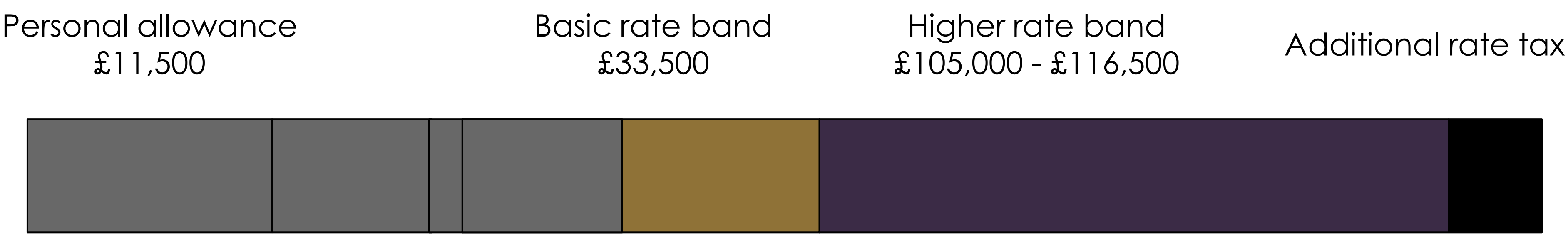
2017/18 TAX BANDS – A HIGH LEVEL OVERVIEW

2017/18 - THE TAX BANDS

- The Personal Allowance
- The Starting Rate Band for Savings
- The Personal Savings Allowance
- The tax free amount for dividends
- Everyone has a £5,000 "tax free" allowance for dividends



- Starting rate band £5,000
- Personal savings allowance £1,000
- Dividend allowance £5,000

Tax free income £22,500

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THE PENDULUM SWINGS BETWEEN COLLECTIVES AND BONDS AGAIN …

For collectives, from 6 April 2016,

Gains in excess of the annual exemption taxed at:

- 10% for Non and basic rate tax payers
- 20% for Higher and additional rate tax payers

Once the dividend allowance of £5,000 is exceeded, the income tax rates are:

- 7.5% for basic rate tax payers
- 32.5% for higher rate tax payers
- 38.1% for additional rate tax payers

Depending upon whether they are onshore or offshore bonds, the tax rate applicable to investment bond gains is:

- 0%, 20%, 25% for onshore bonds or,
- 0% 20% 40%, 45% for offshore bonds

taking into account the client's income tax position.

£5,000 DIVIDEND ALLOWANCE

	2015/16	2017/18	Effective increase
Basic rate	0%	7.5%	7.5%
Higher rate	25%	32.5%	30%
Additional rate	30.55%	38.1%	24.7%

- For those with total dividend income up to £5,000
  BRT – no difference
  HRT – better off (no additional tax liability)
  ART – better off (no additional tax liability)

- For those with total dividend income above £5,000
  BRT – worse off (new 7.5% tax liability)
  HRT – It depends!
  ART - It depends!

SUMMARY – THE CROSS OVER POINT

	Cross over point where taxpayer become worse off in 2017/18 compared to 2015/16
Basic rate taxpayer	£5,000
Higher rate taxpayer	£21,667
Additional rate tax payer	£25,250

Points to consider:

- Remember how the dividend allowance works
- How is the income from your fund classified – interest or dividend?
- Fund mix strategy?
- Do you want income – think about Tapered AA?
- Self Assessment

SUMMARY – THE CROSS OVER POINT

	Cross over point where taxpayer become worse off in 2018/19 compared to 2015/16
Basic rate taxpayer	£2,000
Higher rate taxpayer	£8,667
Additional rate tax payer	£10,100

Points to consider:

- Remember how the dividend allowance works
- How is the income from your fund classified – interest or dividend?
- Fund mix strategy?
- Do you want income – think about Tapered AA?
- Self Assessment

DIVIDENDS AND TRUSTS

- The notional 10% tax credit disappeared entirely from 6 April 2016.
- The £5,000 dividend allowance DOES NOT apply.

Discretionary trusts

7.5% tax on dividends falling within the £1,000 standard rate band.

38.1% tax will apply to dividend income (on dividends above the standard rate band)

IIP/IPDI trusts

7.5% tax liability will apply to dividend income with the life tenant reclaiming/doing nothing/paying more tax to reflect their own tax position

DISCRETIONARY TRUSTS

ACCUMULATION

	2015/16 £	2016/17 onwards £
Dividend	1,000.00	1,000.00
Tax credit	111.11	0
Taxable	1,111.11	1,000.00
Tax liability	416.66	381.00
Net income to the trust	694.45	619.00

This is to be expected as the effective tax rate on the 'net' dividend increased from 30.55% to 38.1%

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Income assumed to be in excess of first £1,000 of Trust income and the settlor is dead

DISCRETIONARY TRUSTS

ACCUMULATION

	2015/16 £	2016/17 onwards £	Investment bond £
Dividend	1,000.00	1,000.00	1,000.00
Tax credit	111.11	0	0
Taxable	1,111.11	1,000.00	0
Tax liability	416.66	381.00	0
Net income to the trust	694.45	619.00	1,000.00

Assuming no changes to investment bond or life fund taxation, bonds will become even more advantageous when compared to trustees holding equities directly or through a collective wrapper.

Income assumed to be in excess of first £1,000 of Trust income and the settlor is dead

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THE CGT ANNUAL EXEMPTION

USING THE ANNUAL EXEMPTION

An initial investment of £188,333 will need to grow by 6% over the year net of charges to make full use of the current CGT annual exemption of £11,300.

Disposal	£199,633
Less original cost	£188,333
Gain assuming 6% growth	£11,300

Issues to consider:

- How long will the investment be held in cash before it is reinvested?
- Will a switch of funds fit in with the investment strategy for the client?
- Will the client be happy to invest in a different fund or funds?
- In reality, does a client tend to invest in a favoured fund for a number of years?
- What will be the charges for purchasing any new funds?

THE VALUE OF THE CGT ANNUAL EXEMPTION…

Tax year	Annual exemption	Tax saved on use of annual exemption	Amount disposed	Max. charge allowed before charges exceed tax saved
2017/18	£11,300	£2,260 (£11,300 @ 20%)	£199,633	1.13%

In 2017/18 if an investment of £188,333 makes a capital gain of 6% over 12 months this results in a gain of £11,300.

For a HRT, if the charge for re-investment is greater than 1.13% the charges will exceed the Capital Gains Tax saved!

For a BRT, the charge for re-investment mustn't be greater than 0.57%!

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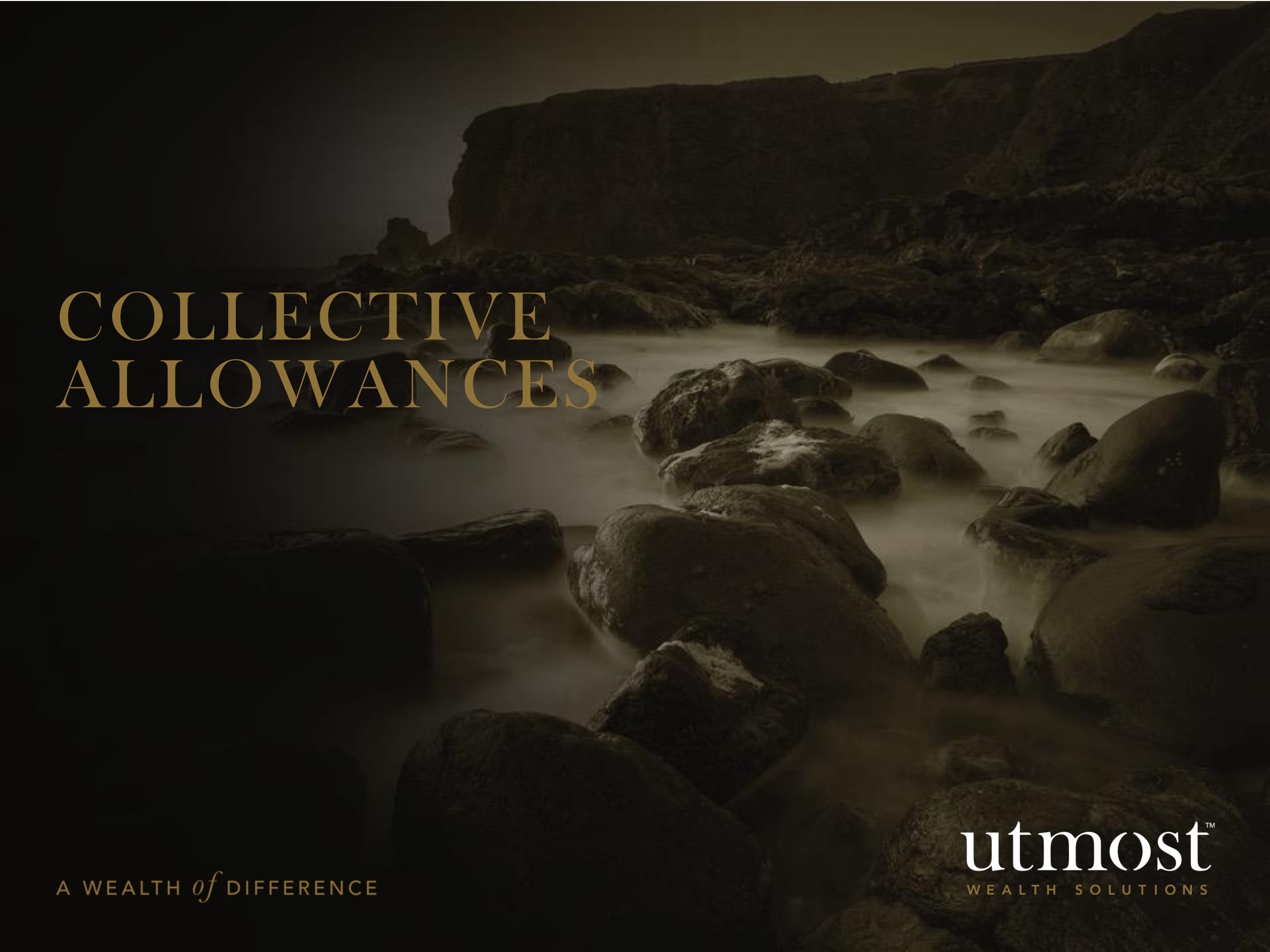

COLLECTIVE ALLOWANCES

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COLLECTIVE INVESTMENT CAPITAL GROWTH

BREACHING THE ANNUAL EXEMPTION

Growth per annum

Initial investment	2%	3%	4%	5%	6%	7%	8%	9%	10%
£113,000	£2,260	£3,390	£4,520	£5,650	£6,780	£7,910	£9,040	£10,170	**£11,300**
£125,556	£2,511	£3,767	£5,022	£6,278	£7,533	£8,789	£10,044	**£11,300**	£12,556
£141,250	£2,825	£4,238	£5,650	£7,063	£8,475	£9,888	**£11,300**	£12,713	£14,125
£161,428	£3,229	£4,843	£6,457	£8,071	£9,686	**£11,300**	£12,914	£14,529	£16,143
£188,333	£3,767	£5,650	£7,533	£9,417	**£11,300**	£13,183	£15,067	£16,950	£18,833
£226,000	£4,520	£6,780	£9,040	**£11,300**	£13,560	£15,280	£18,080	£20,340	£22,600
£282,500	£5,650	£8,475	**£11,300**	£14,125	£16,950	£19,775	£22,600	£25,425	£28,250
£376,667	£7,533	**£11,300**	£15,067	£18,833	£22,600	£26,367	£30,133	£33,900	£37,667
£565,000	**£11,300**	£16,950	£22,600	£28,250	£33,900	£39,550	£45,200	£50,850	£56,500

COLLECTIVE INVESTMENT DIVIDEND YIELD

BREACHING THE DIVIDEND ALLOWANCE

Dividend yield per annum

Initial investment	1%	2%	3%	4%	5%	6%	7%	8%
£62,500	£625	£1,250	£1,875	£2,500	£3,125	£3,750	£4,375	**£5,000**
£71,428	£714	£1,429	£2,142	£2,857	£3,571	£4,286	**£5,000**	£5,714
£83,333	£833	£1,667	£2,500	£3,333	£4,167	**£5,000**	£5,833	£6,667
£100,000	£1,000	£2,000	£3,000	£4,000	**£5,000**	£6,000	£7,000	£8,000
£125,000	£1,250	£2,500	£3,750	**£5,000**	£6,250	£7,500	£8,750	£10,000
£166,667	£1,667	£3,333	**£5,000**	£6,667	£8,333	£10,000	£11,667	£13,333
£250,000	£2,500	**£5,000**	£7,500	£10,000	£12,500	£15,000	£17,500	£20,000
£500,000	**£5,000**	£10,000	£15,000	£20,000	£2,500	£30,000	£35,000	£40,000

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CHARGEABLE GAINS & THE INCOME TAX ALLOWANCES

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CHARGEABLE GAINS

- Chargeable gains from both onshore and offshore bonds are subject to income tax.

- It may be possible to "top slice" gains to reduce the tax due.

- The gain is added to other income in a specific order when calculating the investor's income tax liability.

However,

- Onshore bond gains are added on top of all other income.
- Offshore bond gains are added on top of savings income but below dividends

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CHARGEABLE GAINS

- Why are onshore and offshore bond gains treated differently?
- Onshore bond gains have a 20% tax credit that reflects the corporation tax suffered within the fund.
- As an offshore bond has not suffered tax within the fund (apart from non-reclaimable withholding tax) gains do not have a tax credit.
- Self assessment return forms differentiate between gains from life assurance contracts where tax is "treated as paid".
- http://www.hmrc.gov.uk/forms/sa101.pdf

THE ORDER OF TAXATION

- Income is taxed, and allowances and tax bandings are applied, in a certain order.
- The order of taxation…

Non savings	Savings	Dividends	Chargeable gains
Salary Profits Rents P11D etc.	Bank / BS GILTS Corp Bonds Offshore*	Shares Collectives	Investment bonds Onshore

*On and offshore bond gains are still added after dividends for the purposes of "top-slicing"

2017/18 - THE TAX BANDS

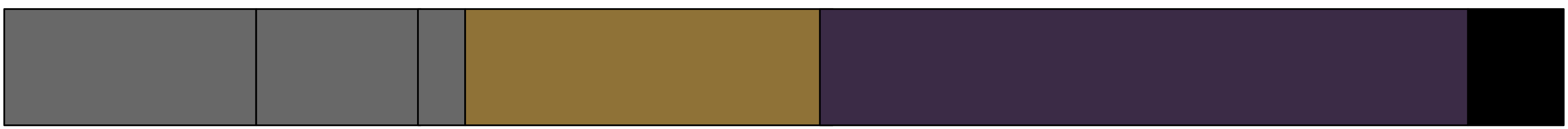
- The Starting Rate Band and Personal Savings Allowance (PSA) are not mutually exclusive
- Both are potentially available
- Consider a client whose non-savings income is within the Personal Allowance but who has significant savings income…

Personal allowance
£11,500

Basic rate band
£33,500

Higher rate band
£105,000 - £116,500

Additional rate tax



Starting rate band £5,000
Personal savings allowance £1,000

Tax free income £17,500

CASE STUDY

Nettie Return and her twin sister Greta are both retired.

They have been self employed all their working lives and each has a basic state pension of £159.55 p.w. (c £8,297 p.a.)

They each have investment portfolios providing them with dividend income of £5,000.00

They each invested into investment bonds which they have recently surrendered.

- Nettie's bond was an onshore bond
- Greta's bond was an offshore bond

NETTIE'S ONSHORE BOND

- Nettie has encashed an onshore bond with a gain of £20,000 (which is deemed to have suffered basic rate tax within the fund).
- She has held the bond for 5 complete years therefore the top-slice divisor is 5.
- The top-sliced gain is therefore £4,000
- Nettie has the standard personal allowance of £11,500.

NETTIE'S NET INCOME

Source of income	Gross	Net
State pension	£8,297	
Dividends	£5,000	
Bond gain	£20,000	
TOTAL	**£33,297**	

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NETTIE'S NET INCOME

Source of income	Gross	Net
State pension	£8,297	£8,297
Dividends	£5,000	£5,000
Bond gain	£20,000	£20,000
TOTAL	**£33,297**	**£33,297**

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GRETA'S OFFSHORE BOND

- Greta has encashed an offshore bond with a gain of £25,000 (higher than the gain under the onshore bond since no UK corporation tax has been deducted within the fund).
- She has held the bond for 5 complete years therefore the top-slice divisor is 5. The top-sliced gain is therefore £5,000
- Greta has the standard personal allowance £11,500.

- Note – there is a 0% "starting rate" of tax which applies to savings income up to £5,000 above the personal allowance as well as a personal savings allowance of up to £1,000.
- The starting rate band is only available for savings income and is lost if taxable earned income exceeds £5,000.

GRETA'S NET INCOME

Source of income	Gross	Net
State pension	£8,297	
Bond gain	£25,000	
Dividends	£5,000	
TOTAL	**£38,297**	

GRETA'S NET INCOME

Source of income	Gross	Net
State pension	£8,297	£8,297
Bond gain	£25,000	£3,203 (£3,203 @ 0%)
		£5,000 (£5,000 @ 0%)
		£1,000 (£1,000 @ 0%)
		£12,638 (£15,797 @ 20%)
Dividends	£5,000	£5,000 (£5,000 @ 0%)
TOTAL	**£38,297**	**£35,138**

SUMMARY

- The net spendable income, after tax, is higher in these examples, where the gain is from an offshore bond.
- Greta has £1,841 more net spendable income than her sister Nettie.
- The offshore bond gains can be offset against the client's personal allowance, her starting rate band (where available) and her personal savings allowance.
- The above case studies simplify the differences between onshore and offshore bond taxation for the purposes of illustration.
- The differences in return will be dependant upon: the underlying investments, the extent to which return is attributed to savings income, dividend income and capital appreciation as well as product costs and charges.

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OFFSHORE BONDS & RETIREMENT PLANNING

THE POWER OF TOP SLICING RELIEF

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RETIREMENT PLANNING

CURRENT STATE OF PLAY

- Minimum pension age is 55
- Annual allowance restricted to £40,000 and as low as £10,000 for some individuals
- Money purchase annual allowance reduced from £10,000 to £4,000 from 06.04.2017
- Lifetime allowance reduced in steps from £1.8m to £1m.
- Transitional protections such as fixed protection can limit/stop funding.

Where next?

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RETIREMENT PLANNING

NOT SO DIFFERENT?

	Pension	Offshore bond
Fund growth	Virtually tax-free	Virtually tax-free
Payments	Tax-relief at highest marginal rate on £3,600 or 100% of relevant UK earnings within annual allowance	No tax relief but no maximum either
Tax-free lump sum	Normally 25% of fund or LTA whichever is lower	*100% of original investment
Income	All income taxed at marginal rate	Only gains taxed at basic, higher or additional rate
Reliefs	Personal allowance	Personal allowance Starting rate band Personal savings allowance Top slicing Time apportionment Tax free assignment

*As part of full surrender/included in chargeable event calculation

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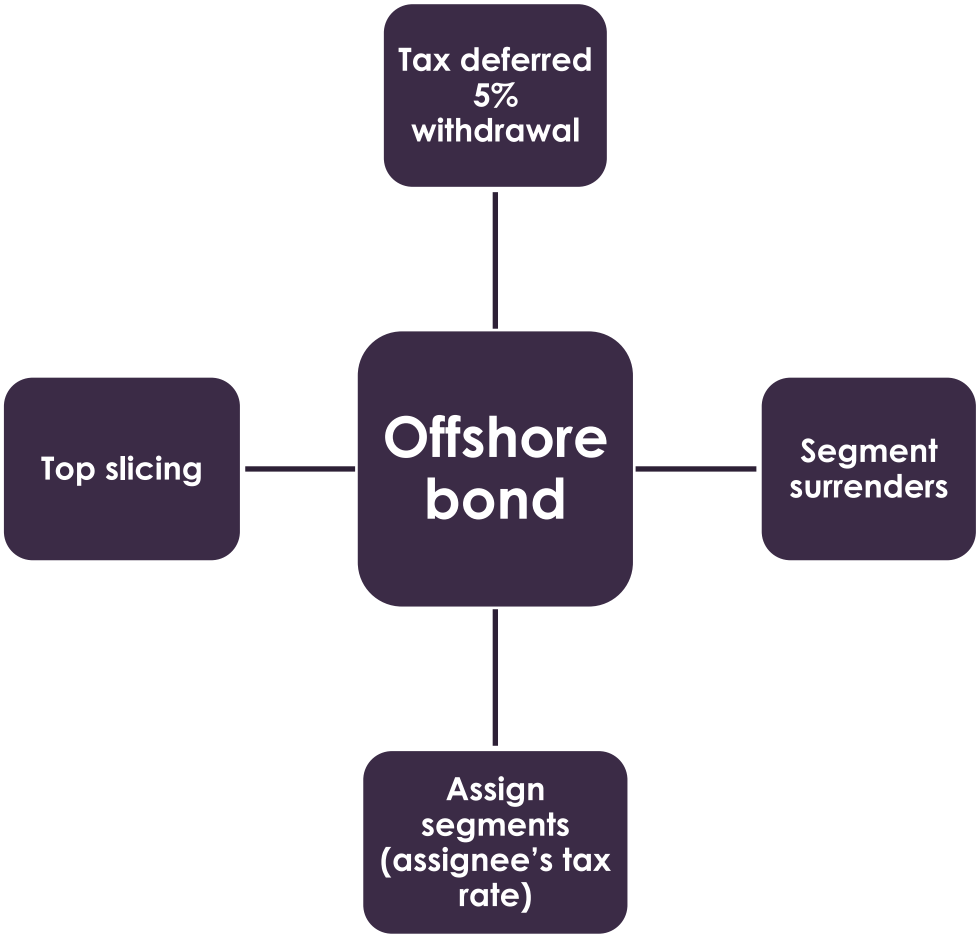
TAX EFFICIENT "INCOME"

- Top slicing only used where client is not already a higher or additional rate tax payer
- Not available to trustees
- Averages gain over the period of investment
- Add averaged gain to the individual's income in the year of encashment to determine higher/additional liability.



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TOP SLICING

MAXIMUM GAIN WITH NO HIGHER RATE TAX

- If investor, or assignee, had no UK income in the year of encashment, the effect of top slicing would mean that the following gains could be realised with no liability to higher rate tax…

Year of Benefit	Possible gain before pay HRT	
	2017/18	**Top slice**
After 1 year	£45,000	£45,000
After 2 years	£90,000	£45,000
After 5 years	£167,500	£33,500
After 10 years	£335,000	£33,500
After 15 years	£502,500	£33,500
After 20 years	£670,000	£33,500

- However, adjusted net income in excess of £100,000 means that personal allowance is lost on a 2 for 1 basis.

TOP SLICING

MAXIMUM GAIN WHILST PRESERVING PERSONAL ALLOWANCE

- If the personal allowance is to be maintained, the chargeable gain should be limited to £100,000 where an individual has no other income

- Bond gains are included in the adjusted net income calculation and top slicing does not apply

Year of Benefit	Possible gain before reducing personal allowance	
	2017/18	**Top slice**
After 1 year	£45,000	£45,000
After 2 years	£90,000	£45,000
After 5 years	£100,000	£20,000
After 10 years	£100,000	£10,000
After 15 years	£100,000	£6,667
After 20 years	£100,000	£5,000

- The full personal allowance then remains available.

RETIREMENT PLANNING

THE POWER OF TOP SLICING RELIEF

- Bill is aged 67 and is receiving gross income of £60,000 p.a. consisting of:

State Pension	£10,000
Drawdown	£40,000
Interest/coupons	£10,000
	£60,000

- His drawdown fund is worth £500,000 and he is married with two adult children.
- In addition, he holds an offshore bond that he invested £500,000 into 10 years ago, following receipt of an inheritance. It is now worth £1,000,000 and he has never taken any withdrawals.

How could the offshore bond be used to increase tax efficiency in retirement?

CURRENT TAX POSITION

	Non Savings	Savings	Total
State pension			
Drawdown			
Interest/Coupons			
Total			
Less personal allowance			
Total			
£? @ 20%			
£? @ 40%			
£? @ 0%			
£? @ 40%			
Total tax on income			
Net spendable income			
Effective tax rate			%

CURRENT TAX POSITION

	Non Savings	Savings	Total
State pension	£10,000		
Drawdown	£40,000		
Interest/Coupons		£10,000	
Total	£50,000	£10,000	£60,000
Less personal allowance	(£11,500)		
Total	**£38,500**	**£10,000**	**£48,500**
£33,500 @ 20%		(6,700)	
£5,000 @ 40%		(2,000)	
£500 @ 0%		(0)	
£9,500 @ 40%		(3,800)	
Total tax on income			**(£12,500)**
Net spendable income (£60,000 - £12,500)			**£47,500**
Effective tax rate (£12,500/£60,000)			**20.83%**

What if Bill switched off his drawdown income and used his bond encashment to match his net spendable income of £47,500?

MATCHING NET SPENDABLE INCOME

Encash £31,111 of the offshore bond and create a chargeable event of £15,555…

	Non Savings	Savings	Total
State pension			
Interest/Coupons			
Bond gain			
Total			
Less personal allowance			
Total			
£? @ 0%			
£? @ 0%			
£? @ 20%			
£? @ 20%			
Total tax on income			
Net spendable income			
Effective tax rate			%

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MATCHING NET SPENDABLE INCOME

Encash £31,111 of the offshore bond and create a chargeable event of £15,555…

	Non Savings	Savings	Total
State pension	£10,000		
Interest/Coupons		£10,000	
Bond gain		*£15,555	
Total	£10,000	£25,555	£35,555
Less personal allowance	(£10,000)	(£1,500)	
Total	£0	£24,055	£24,055
£5,000 @ 0%		(0)	
£1,000 @ 0%		(0)	
£2,500 @ 20%		(500)	
£15,555 @ 20%		(3,111)	
Total tax on income			**(£3,611)**
Net spendable income (£51,111 - £3,611)			**£47,500**
Effective tax rate (£3,611/£51,111)			**7.06%**

*Total income including top sliced gain of £1,555 = £21,555 therefore no higher rate tax liability on bond encashment.

NSI maintained…..but tax bill reduced by 71.11%!

MATCHING THE TAX BILL

Encash £119,000 of the offshore bond and create a chargeable event of £59,500…

	Non Savings	Savings	Total
State pension	£10,000		
Interest/Coupons		£10,000	
Bond gain		*£59,500	
Total	£10,000	£69,500	£79,500
Less personal allowance	(£10,000)	(£1,500)	
Total	£0	£68,000	£68,000
£5,000 @ 0%		(0)	
£500 @ 0%		(0)	
£3,000 @ 20%		(600)	
£59,500 @ 20%		(11,900)	
Total tax on income			**(£12,500)**
Net spendable income (£139,000 - £12,500)			**£126,500**
Effective tax rate (£12,500/£139,000)			**9.00%**

*Total income including top sliced gain of £5,950 = £25,950 therefore no higher rate tax liability on bond encashment.
Note that the bond gain reduces personal savings allowance to £500.

Same £12,500 tax bill….but NSI increased by 266.32%!

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SUMMARY

THE POWER OF TOP SLICING

- Where income levels can be managed in retirement, offshore bonds can represent a highly efficient source of "income", especially where top slicing relief is utilised
- The level of chargeable events achievable following segment surrenders will depend upon the amount of growth achieved and the number of segments
- Chargeable events could also be created with excess 5% withdrawals
- This strategy can potentially save income tax or increase net spendable income levels however care should be taken that:
  - Adjusted net income does not exceed £100,000 when combined with chargeable gain
  - The higher rate threshold is not exceeded when the top sliced gain is combined with other income
- The pension fund is also not depleted meaning that the legacy for future generations is potentially increased!

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THE POWER OF NUMBERS

CASE STUDY

Dai Versify is aged 60 and has the following investments;

- Uncrystallised SIPP with a value of £1 million with no form of fund protection
- Offshore Investment Bond valued at £500,000
  - Original investment £250,000, with 250 segments, made from an inheritance 10 years ago
  - No previous withdrawals
- ISA portfolio valued at £500,000
- OEIC portfolio valued at £500,000
  - Amount invested £240,000

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CASE STUDY

Investment and Pension Wealth = £2.5 million

Dai is looking to take a net £100,000 income in 2017/18.

How much of his investments do you think he will need to use and what do you think his effective rate of tax will be?

£100,000 TAXABLE INCOME IN 2017/18

For somebody with "taxable" income of £100,000 this is the impact;

	Amount	Tax rate	Tax payable
Personal allowance	£11,500	0%	Nil
Basic rate band	£33,500	20%	£6,700
Higher rate band	£55,000	40%	£22,000
Totals	£100,000	28.7%	£28,700

How can Dai's tax wrappers help to minimise his tax exposure whilst meeting his "income" objectives?

"INCOME"

Generated by the tax wrappers;

- Pension - Nil
- Offshore Bond - £50,000
- OEIC - £5,000 dividend income p.a. plus £21,000 part disposal
- ISA - £26,000 capital drawdown

Total £102,000

Is this really enough to provide Dai with a net income of £100,000?

TAX

Assumptions;

Personal allowance of £11,500

- Full Bond gain of £25,000 when added to other taxable income is within £100,000 so the personal allowance is retained!

Taxable income;

- Offshore Bond = £25,000
- Dividend income = £5,000
- **Total = £30,000**

INCOME TAX – 2017/18

Source	Savings £	Dividend £	Total £
Offshore	25,000.00		
OEIC		5,000.00	
Total	**25,000.00**	**5,000.00**	**30,000.00**
Less P.A.	(11,500.00)		
Less £6,000 @ 0%	(6,000.00)		
Taxable income	7,500.00	5,000.00	12,500.00
7,500 @ 20% = 1,500			
5,000 @ 0% = 0			
Total income tax			**1,500.00**

Bond top-sliced gain within basic rate band, so no further tax due. The part disposal is within the CGT annual exemption

Dai Versify's total tax = £1,500

Remaining basic rate tax band £12,500 where no earned income

(£33,500-£13,500-£5,000-£2,500 top slice gain on bond)

THE POWER OF TAX WRAPPERS

- Pension and Investment Wealth of £2.5 million
- **Producing gross "income" of £102,000 and a net "income" of £100,500!**
- **Effective tax rate of 1.47%** (£1,500/£102,000)

What if we were advising a couple?

- Double the asset wealth!
- Double the "income"
- But still with an effective tax rate of 1.47%!
- Flexibility provided by tax legislation, both with regard to offshore bonds and pensions
- Combined with a strategic wrapper allocation that provides choice, flexibility and control for changing tax legislation and personal circumstances in future…

TAX WRAPPERS COMBINED – CONSISTENT?

2014/15

- Lower Personal Allowance
- No Personal Savings Allowance
- Tax bill £2,455
- Tax rate **2.39%**

2015/16

- Lower Personal Allowance
- No Personal Savings Allowance
- Tax bill £2,435
- Tax rate **2.37%**

2016/17

- Lower Personal Allowance
- Tax bill £1,600
- Tax rate **1.57%**

The rates are different – but consistently low by combining tax wrappers

DAI'S ALTERNATIVE STRATEGY

WITHOUT ADVICE

WRAPPER	INCOME £
SIPP (UFPLS)	125,000 (93,750 taxable)
ISA drawdown	Nil
Part disposal of collectives	Nil
Collectives dividend yield	5,000
Offshore bond segment surrender	Nil
Total	**130,000**

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TAX

Assumptions;

- Personal allowance of £11,500

Taxable income;

- Pension Income = £93,750
- Dividend income = £5,000
- **Total = £98,750**

INCOME TAX – 2017/18

Source	Non savings £	Dividend £	Total £
Pension	93,750		
OEIC yield		5,000.00	
Total	**93,750.00**	**5,000.00**	**98,750.00**
Less P.A.	(11,500.00)		
Taxable income	82,250.00	5,000.00	87,250.00
33,500 @ 20% = 6,700			(6,700)
48,750 @ 40% = 19,500			(19,500)
5,000 @ 0% = 0			0
			£72,550

Dai Versify's Total Tax = £26,200

Total net "income" = £31,250 PCLS + £72,550 = £103,800

Effective tax rate = 20.15% (£26,200/£130,000)

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ESTATE PLANNING AND IHT

Original strategy	Tax wrapper	Alternative strategy
£1,000,000	SIPP	£875,000
£450,000	Offshore Bond	£500,000
£474,000	ISA	£500,000
£479,000	Collectives	£500,000
£2,403,000	**Gross Estate**	**£2,375,000**
£1,403,000	Taxable Estate	£1,500,000
£325,000	NRB	£325,000
£1,078,000	Net Taxable	£1,175,000
£431,200	Tax@40%	£470,000
£1,971,800	**Net Estate**	**1,905,000**

Assumptions; After first annual withdrawal from tax wrapper, Pension is free of IHT, ISA is not invested in AIM shares, Dai is single

£66,800 more for beneficiaries in first year!

PENSIONS AND OFFSHORE BONDS

The increased personal allowance, the starting rate band and net "interest free amount" for savings income from 2017/18 are of most use with an offshore bond surrender to provide retirement income when there is little or no earned income;

- Before state pension age
- Before taking private pensions

PENSIONS AND OFFSHORE BONDS

Whilst it will be known when state pension will start and for what amount the interaction between private pensions and offshore bonds as post retirement vehicles will depend upon a number factors which include;

- Death benefit tax charges on pensions in future
- Interaction of PCLS and pension
- Relative size of Offshore Bond and Pension funds
- Other non savings income e.g. rental income
- Whether there is a spouse and their tax position

LEARNING OBJECTIVES

By the end of the session delegates will be able to;

- Appreciate some of the high level differences between certain investment tax wrappers including:
  - The internal taxation
  - The availability to clients of certain income tax allowances
  - The tax planning opportunities presented by a portfolio of multiple tax wrappers within a client portfolio.
- Be able to discuss and explain this subject with a client in a clear and concise way
- Apply this knowledge to appropriate, individual, client scenarios.

UTMOST WEALTH SOLUTIONS

SUMMARY

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UTMOST TRUST RANGE

- **Discounted Gift Trust** (Absolute and Discretionary)
- **Loan Trust** (Discretionary) (+ deed of waiver availability)
- **Discretionary Gift Trust** (Settlor can and cannot be a potential beneficiary)
- **Absolute Gift Trust** (Settlor can and cannot be a potential beneficiary)
- **Probate Trust**
- **Excluded Property Trust**
- **Appointment of beneficial interest to create bare trust for a minor** (when distributing discretionary trust assets to a minor)

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CII NOTTINGHAM SEPTEMBER 2017

THANK YOU FOR YOUR TIME

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IMPORTANT INFORMATION

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International bonds are intended to be a medium (at least 5 years old) to long term (over 10 years) investment. The value of investments may fall as well as rise and is not guaranteed. Your client or their trustees may get back less than originally invested.

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