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Pensions issues for law firm partners

Applicable at 14 August 2017

Introduction

The ever change world of pensions

Howard Hackney

Howard escaped from Grant Thornton UK LLP in 2008 where he had been a partner for over 25 years to establish his own boutique practice. During his time at Grant Thornton he was head of professional practices for the North West and head of family businesses for the UK. At Grant Thornton he had a variety of roles including office Managing Partner, North West regional marketing partner and membership of the partners appointments panel. Howard specialises in advising mid market professional practices and family businesses. In 2002 he won the CBI's national award as "Best Business Adviser“.

Howard's current focus is providing "special projects" advice to family businesses with turnovers up to £30m and professional firms with up to 20 partners. His experience extends from first generation to eighth generation family businesses with all the succession issues that involves.

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Mark Waddilove

Mark Waddilove is the tax partner in charge of the professional services tax team at RSM. He deals with a wide range of issues relating to partnerships, limited liability partnerships (LLP) and the private client tax affairs of the partners including tax efficient business structuring, remuneration strategies, international tax, and succession planning, as well as overseeing the personal tax compliance function of the partners' tax affairs.

He has been with RSM since November 2010. Mark is a partner with nearly 30 years' partnership and LLP experience gained at HM Revenue and Customs, Smith & Williamson and nearly 25 years with EY and PwC. He is a member of the Chartered Institute of Taxation, a member of the Association of Professional Practitioners and chairs the firm's partnership tax steering committee. Mark currently leads the firm's partnership and business tax planning group and has considerable experience in developing bespoke alternative business structures for the firm's clients. He works closely with many of RSM's overseas associated firms to deliver a coordinated approach for our international clients.

Mark regularly contributes articles and gives presentations on key issues facing professional service firms, such as structures and tax planning. His clients include those in the legal sector, property consultants including architects and engineers, the financial services sector and management consultants.

Outside of work Mark and has two children, Alexander, Emily and not forgetting the family black Labrador. Apart from unpaid taxi services for the children, Mark can be found either on the golf course where his keen enthusiasm for the game is not reflected in his ability or on his road bike attempting to be the next Bradley Wiggins.

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Agenda

- An overview *(NB we are considering defined contribution schemes only)*
- Establishing the fund
- Building the fund – including buying commercial premises
- Drawing on the fund – personally & for the next generation

Overview

A personal view

- Self administered arrangements almost a "no brainer"

- Genuine independent provider
  - Control
  - Flexibility
  - Advice
- In spite of recent changes still strong belief in pension planning
  - Tax benefits
  - Security for the individual
  - Succession planning (both personal and for the partnership)
- Complex
  - But do not be put off
  - Take specific advice as lots of technicalities

Establishing the fund

SIPP or SSAS

- SIPP (self-invested personal pension) – personal arrangement – FCA regulated
- SSAS (small self administered scheme) – company arrangement - which many will not have
- Virtually the same - except
  - SSAS is more complex & can be more costly if few members but has greater investment flexibility
  - SSAS can make loan backs repayable over 5 years of up to 50% of fund (secured with 1st charge)
  - SIPP can buy up to 50% of connected company (SSAS only 5% of the fund value)
  - SASS can make loans to a connected party without a tax charge
  - SSAS is “your scheme”, rather than a SIPP governed by a particular provider – members are trustees
  - SIPP is FCA regulated, SSAS is not (how long?) but subject to regulation of the Pensions Regulator
  - SSAS not covered by the FS compensation scheme

Tax benefits (within limits – see below)

- Limits
  - Annual contributions £40k - £10k
  - Lifetime limit £1m
- On personal contributions
  - Income Tax relief on contributions at marginal rates
  - But make sure sufficient taxable income
- On company contributions
  - Corporation tax relief
  - No longer a concern about salary levels (justifiable)
  - Company can “control” level of income for restriction on relief
- While monies are within the pension fund
  - Tax free growth
  - Usually protected in a bankruptcy but not divorce

Tax benefits (within limits – see below) ctd.

- When drawing benefits
  - 25% of pension fund available as tax free lump sum
  - Income Tax payable at point of taking taxable income
  - Taxed at marginal rate of recipient
- On death
  - Fund is free of tax if death before age 75
  - If death post 75 then beneficiaries pay Income Tax on withdrawals

Adviser roles

- Accountant
  - Tax position
  - Available relief in conjunction with scheme provider
  - Strategic options (tax rates)

- Strategic wealth adviser (independent?)
  - Advice on selecting an appropriate provider
  - Investment advice
  - Advice on balance between other forms of retirement savings and pension savings (both accumulation and decumulation)
- Scheme provider
  - Technical advice
  - Keep you within rules
  - Flexibility
- Dedicated investment manager
  - No actual need
  - Difficult to justify if fund < £100k

Pension v ISA – balance in everything

	ISA	Pension
Tax relief on contributions	No	Yes
Tax free growth	Yes	Yes
Tax free access	100%	25%
Potentially IHT free	Maybe	Yes

- ISAs (investment savings allowance) made more complex in recent years
  - Cash or stocks & shares
  - Lifetime ISA ("Lisa")
  - Help-to-buy ISA
  - Junior ISA ("Jisas")
- Now £20k p.a. for an ISA, £4,128 Jisa and £4k for Lisa
- But the future of pensions?
- Personal investment companies?

Building the fund

Contributions

- From 6/4/14 £40k gross "Annual Allowance"
- Unless "adjusted income" > £150k → by £210k only £10k gross (£2 for £1 reduction)
- Carry forward from three previous years – if have existing scheme in place (LIFO) but beware of 2015/16!
- If nil contributions in 3 prior years £160k now (£40k + £40k + £40k + £40k)
- Watch level of income to relieve at 40%/45%
- Personal contributions pay net of 20% - Limited to 100% of earned income
- Employer contributions pay gross
  - Contributions count as earnings for "adjusted salary"
  - If threshold earnings < £110k no need to consider

Lifetime Allowance

- Prior Allowances
  - Unlimited until 5/4/2006
  - £1.5m to £1.8m between 5/4/2006 and 5/4/2012
  - £1.8m until 5/4/2012
  - £1.5m until 5/4/2014
  - £1.25m until 5/4/2016
  - £1m from 6/4/2016
- Excess charged at 55% at point of drawing (25% if retained within pension)
- Take care over when to cease contributions – many already have
- Protection is available if contributions cease & election made
- Election for £1.25m protection if conditions met – but watch admin.
- Watch growth relative to allowance, but the £1m will be indexed from 2021
- Final salary schemes usually valued as 20X final salary.

Investment flexibility

- Traditional stocks & shares (including options) allowed
- Commercial (non-residential) property allowed
- Unlisted shares allowed
  - Difference between SIPP/SSAS
  - Differences between connected and non-connected
  - Do you have control, if so watch impact of “taxable property”
  - Very complex & not seen often but most often used for short term equity release
- “Exotics” e.g. cars, wine, stamps and tangible moveable property generally not advised as significant tax charges
- Same applies to residential property (possible via a fund)

Commercial property

- Consider purchasing company premises with pension
  - Effective purchase at 40%/45% discount
  - Rental returns of 5%-10%
  - Tax free growth
  - Control of destiny
  - Can release cash from existing pensions if property already owned
- Can borrow up to 50% of fund
- Can use existing pension funds – but take care over transfers
- Open market rent payable tax free to the pension scheme
- Timing can be an issue too (e.g. tax refund within SIPP, VAT)
- Partnership issues
  - Can buy <100%
  - Need for agreement with partners on exit & % share arrangements

Commercial property example (assumed 40% taxpayer)

Cost of property	£500,000
Net contribution	£96,000
Tax reclaim via Self Assessment (can be a time lag)	£32,000
Tax relief at source	£32,000
Gross contribution	£160,000
Existing funds transfer in	£174,000
Total fund value	£334,000
Borrow 50% of the fund	£166,000
Total funding	£500,000

Remember to account for costs (e.g. Stamp Duty, legal fees, valuation fees, admin fees) and ongoing regulatory compliance fees

Drawing on the fund

Retirement Options

- Applies post age 55 (current minimum retirement age)
- 25% tax free
  - Phased due to IHT benefits
  - OR fully taken
- Three options
  - Buy annuity
  - Access the fund directly
  - A mixture
- Guaranteed Annuity Rates (GAR) “trap”
  - Older policies tend to have these, which can be very beneficial
  - **But “traps”**– e.g. single life, non guaranteed, payable in arrears, no escalation
  - Potential to take a GAR & insure to mitigate the effects of some of these traps

Strategy when accessing benefits

- No longer is taking pension at retirement date default position
- Old maxim “tax deferred is tax saved”
- Leave in fund until needed as sheltered from IHT (under 75 years old)?
- Extracted tax free lump sum → falls within estate (potentially subject to IHT)
  - unless spent
  - OR successfully used for IHT planning
- Take tax free lump sum in stages sufficient to meet living needs? Leaving remainder sheltered from IHT?
- Then take income?
- Consider tax treatment of personal assets (including ISA funds) vs pension assets

Accessing benefits directly

- "Flexi access drawdown"
  - 25% tax free
  - 75% balance available to withdraw at will, subject to marginal rate of Income Tax
  - Usually flexibility to access proportionately (phased)
- Options – complex IHT v Income tax

	Phased	Full 25%
Fund value	100,000	100,000
Tax free	10,000	25,000
Taxable income	18,000	-
Assumed tax	(3,000)	-
Net income	25,000	25,000
Fund remaining	72,000	75,000
Income tax free element	15,000	-
Subject to income tax when drawn	57,000	75,000

- Not all pension policies offer drawdown

Impact of death on fund

- Old rules pre 5/4/15
  - Pre 75 IHT free if non vested
  - Death pre 75 & vested – 55% tax charge → phased retirement often encouraged
  - Death post 75 – 55% tax charge (was 82%)
- New rules only two situations
  - Death < age 75 → no tax on amounts equal to LA (55% on excess)
  - Death > age 75 → beneficiaries pay Income Tax on withdrawals
- Payable to "anyone"
  - Lump sum or pension
  - Surviving spouse
  - Children
  - Trusts

Presenters

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