



Chapter 8 – Lifetime Financial Provision

13 Questions



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Retirement Planning Process



**Key stages
of the
retirement
planning
process**

**Why
retirement
planning is
important**



Information Needed

In addition to basic client information will need

- Anticipated retirement date
- Current assets and investments
- Expected lump sum payments from any existing pension arrangements
- Estimates of the income they can expect from any existing pension arrangements
- The amount of any state pension that might be payable
- What level of cash reserves the client will need for emergencies and the unexpected

In order to develop a strategy from this will need to identify

- An estimate of any lump sum that may be needed at retirement to repay items such as mortgages or to fund things such as special holidays
- An estimate of the income they will need in retirement taking into account inflation





Intended retirement age

Need to establish normal retirement age for any existing pension products

Does the pension plan permit earlier or later retirement



Client's aspiration

At what age is the client hoping to retire

How does the client's aspiration match with their pension plans

What number of years will their retirement savings need to fund



Occupational Pension Schemes

Defined Benefit Scheme

AKA *final salary scheme* where the pension is related to the number of years of service and the individual's final salary.

Offers a promise on income until death, usually.

Reliant on the employer as investment risk sits with them.

Defined Contribution Scheme

The pension provided is related to the contributions made and investment performance achieved. For e.g., 401K scheme.

Contributions are invested.

Fund size depends upon investment performance.



Quantifying Needs

- Lifestyle and intended retirement age will drive the retirement funds that the client needs to accumulate to meet their expectations
- Assessment of income and capital needs
- Using present and future value calculations to estimate size of retirement funds needed

$$\textit{Present Value} = \frac{\textit{Terminal Value}}{(1 + r)^n} \quad \textit{Future Value} = \textit{Present Value} \times (1 + r)^n$$



Types of Pension Products

Pension plans

- Tend to receive favourable tax treatment - tax relief on contributions and either exemption or additional allowances against tax on gains and dividend income
- Pension plans can often provide a better investment vehicle for meeting clients' needs

Types of pension plans

- State pension
- Defined benefit
- Defined contribution
- Personal pensions

Need to assess benefits they will generate, scope for any additional contributions and suitability of retention



Retirement Planning Strategies

Funds needed for retirement are likely to come from a combination of pensions, savings, investments and other assets

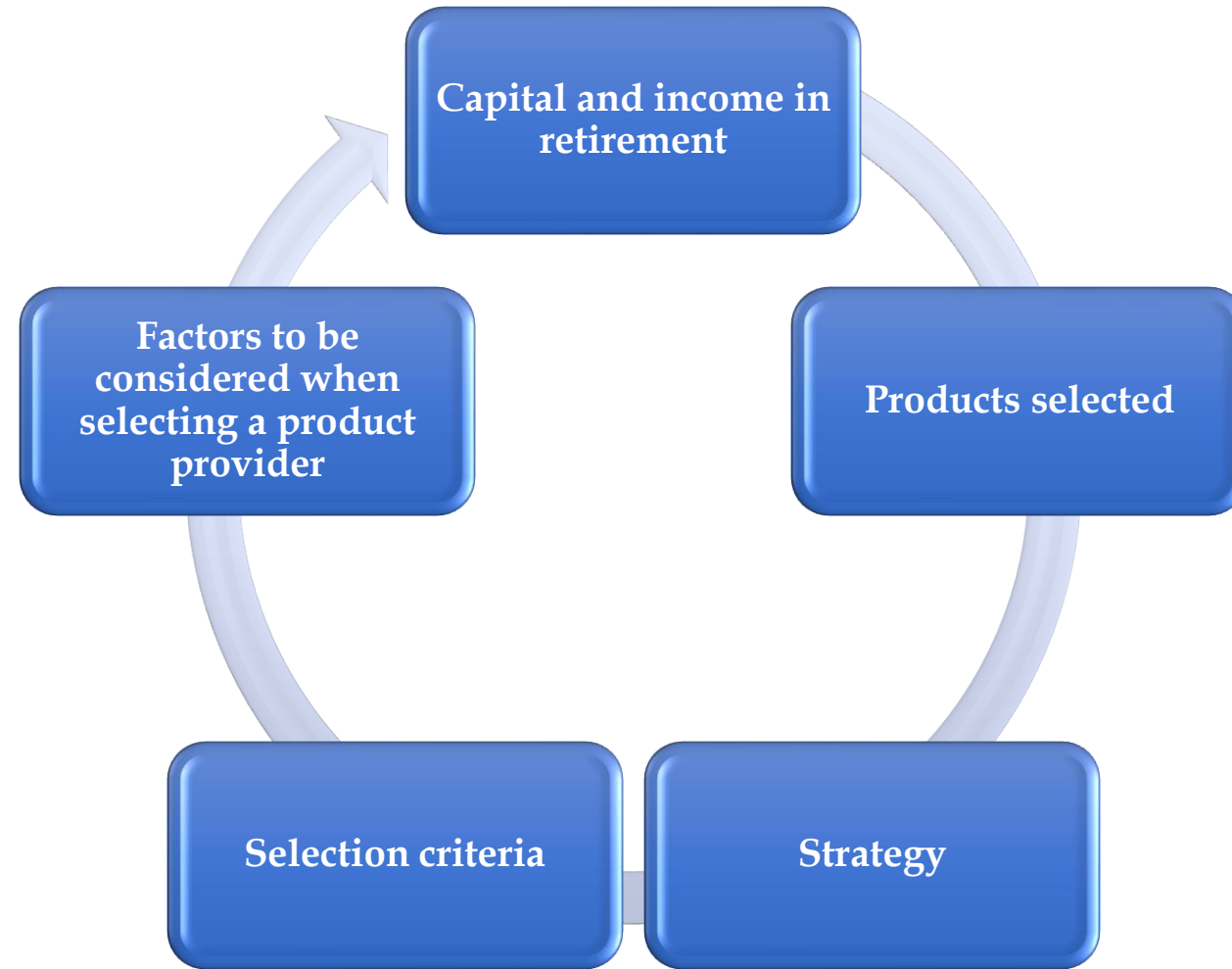
Key is a coordinated investment strategy that will generate income and capital needed at retirement

Strategy will vary with stage of life

- Under 40/50
- As retirement approaches
- At retirement



Retirement Plan





Report will need to cover:

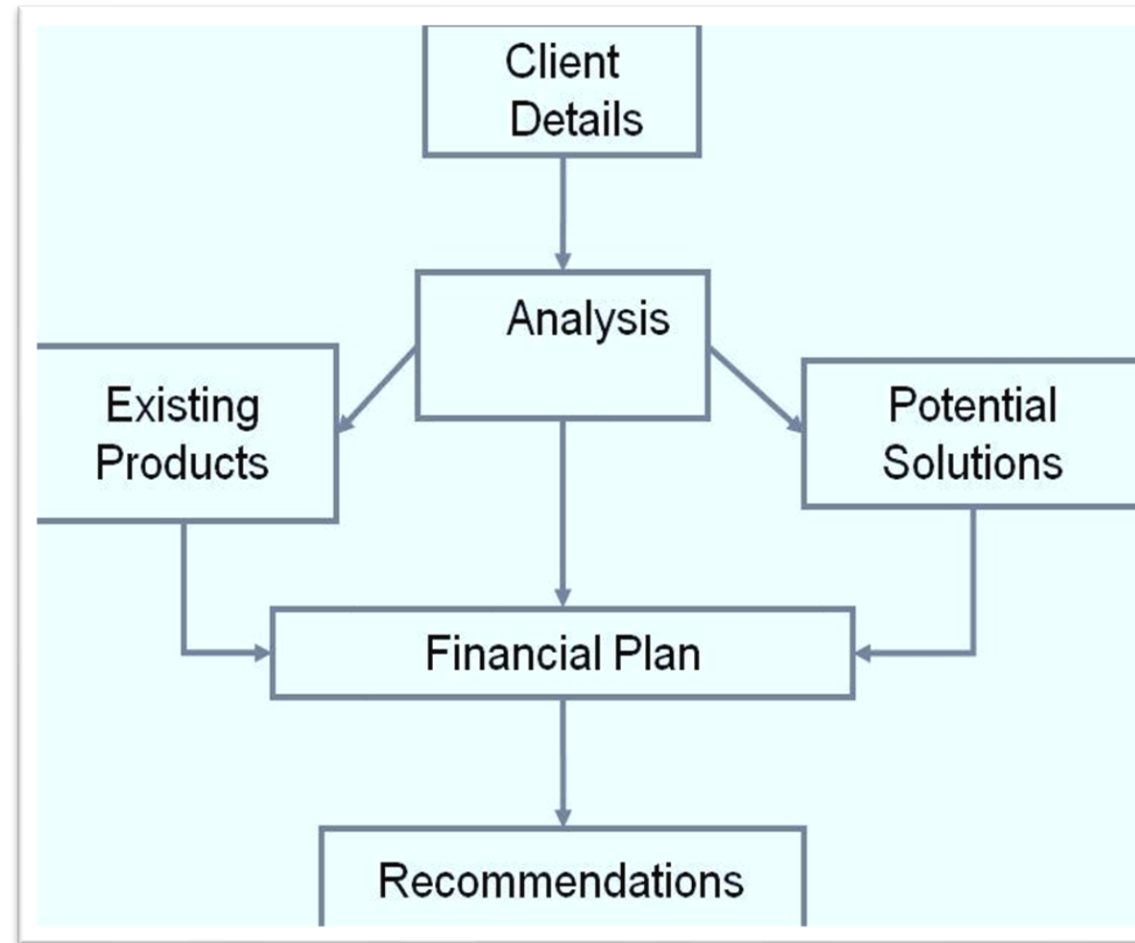
Income

Capital

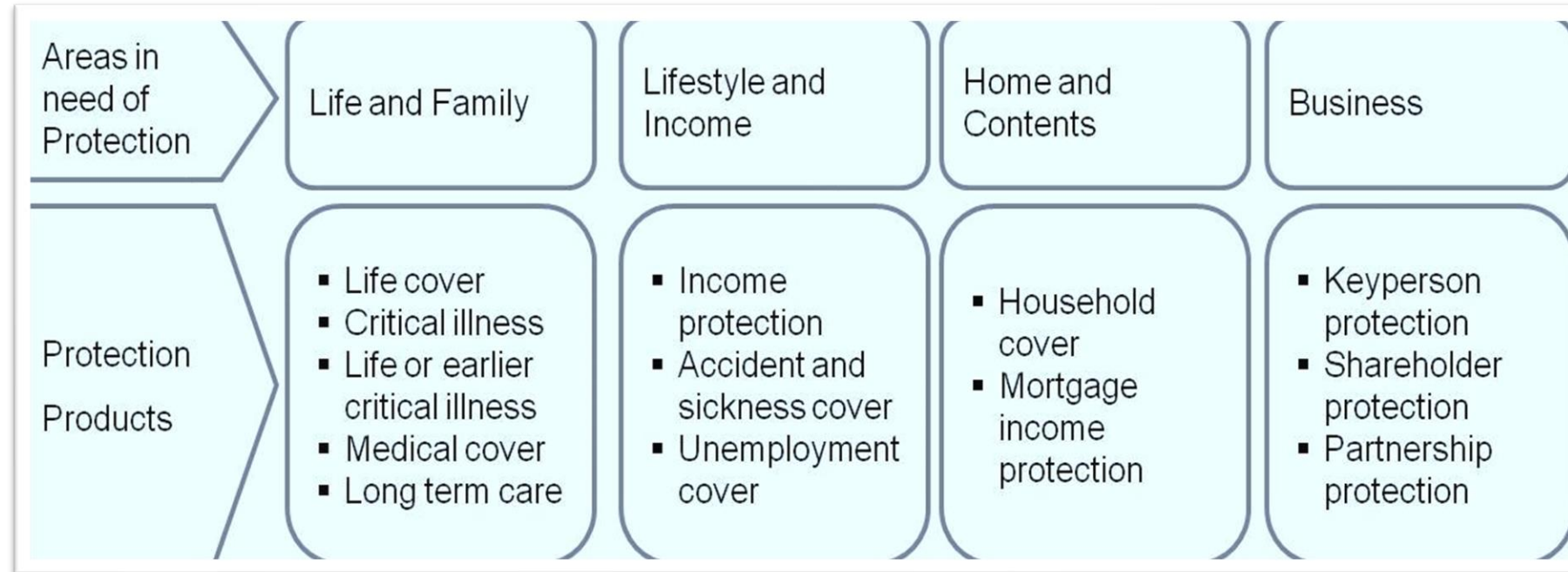
Protection



Protection Planning



Main Protection Areas



Prioritisation Process

Area of Need	What could Happen	Potential Impact
Life and Family	<ul style="list-style-type: none"> ▪ You suffer a fatal heart attack ▪ You are diagnosed with a critical illness ▪ You or someone in your family needs surgery ▪ You are unable to look after yourself and need full time care 	<ul style="list-style-type: none"> ▪ Your family lose your income and have insufficient funds to live on ▪ You face major medical bills and care costs ▪ You may want immediate access to a private hospital ▪ The cost of care exhausts all of your savings
Lifestyle and Income	<ul style="list-style-type: none"> ▪ You lose your main source of income ▪ You suffer an accident or sickness that prevents you working ▪ You lose your job 	<ul style="list-style-type: none"> ▪ Your savings are insufficient to maintain your lifestyle ▪ Benefits from the state or your employer are insufficient ▪ It takes a long time to find a new job and you exhaust your savings
Home and Contents	<ul style="list-style-type: none"> ▪ Your home is flooded ▪ You lose you job ▪ You die before your mortgage is repaid 	<ul style="list-style-type: none"> ▪ Major expenditure to repair the damage and buy new contents ▪ You are unable to meet your mortgage repayments ▪ Your family are saddled with ongoing mortgage repayments
Business	<ul style="list-style-type: none"> ▪ A key person in your business dies ▪ A shareholder dies ▪ A partner is no longer able to work 	<ul style="list-style-type: none"> ▪ The business can no longer generate its products or sales ▪ Their shareholding needs to be bought out ▪ Their share of the partnership needs to be bought out



Prioritisation Process

Simply because a need has been established does not mean that it can be addressed

Affordability will be a major constraint on a client's ability to protect against all of the risks that might arise

Planning & prioritisation process



Assessing suitability

- Relevance to needs
- Extent of the cover and whether adequate
- Whether an option for cover to be extended
- Are they affordable options
- Can client afford to increase what is paid
- Whether the original timescale is still valid
- Risk associated with the product against the client's risk tolerance
- Extent of any diversification or lack of
- Level of charges compared to comparable products



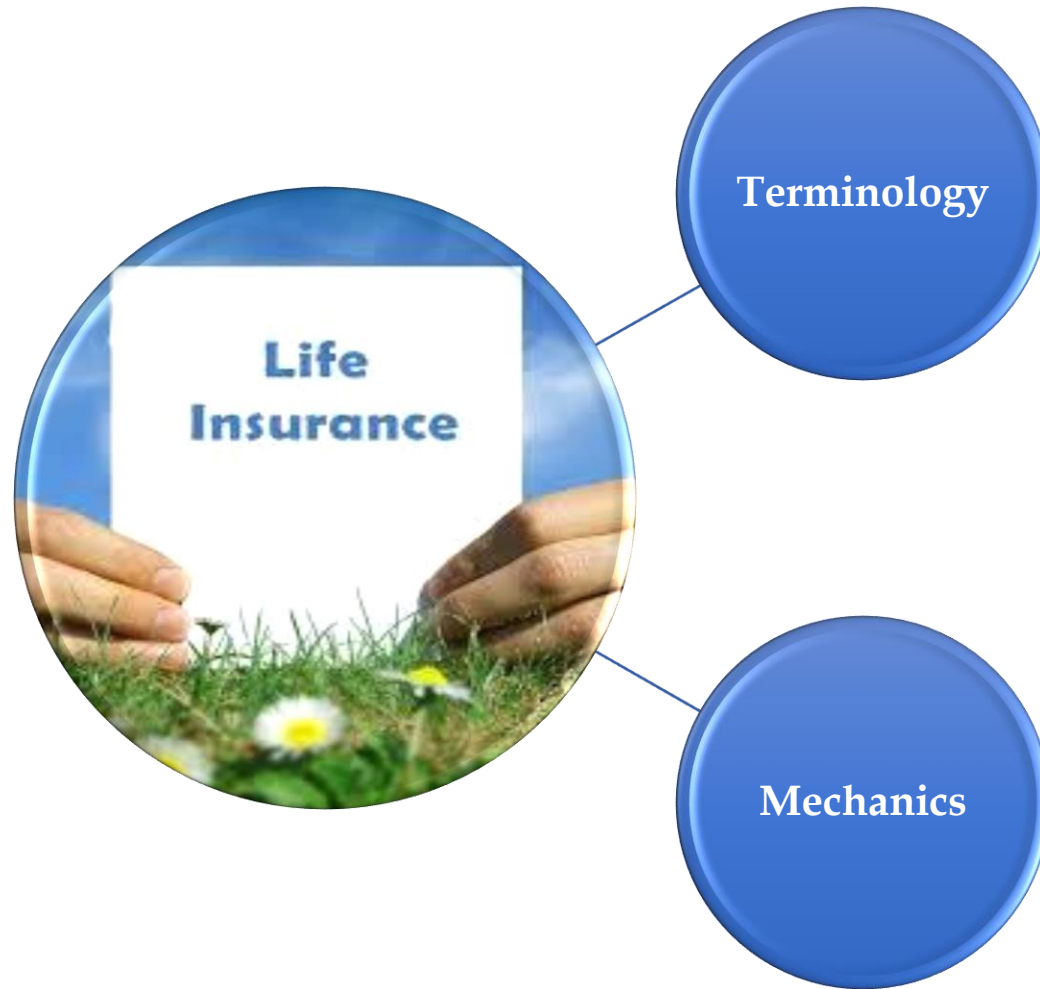
Develop an income and expenditure plan

Quantify need by asking

- **If the client or partner were to die**
- **If the client or partner become unable to work**
- **Who would look after the home or the children if the client or partner were unable to**

May then indicate that it is necessary to replace not just lost income but to generate additional income or a capital sum





- Proposers
- Lives assured
- Single and joint life policies

- Proposal
- Utmost good faith
- Disclosure
- Underwriting
- Cancellation rights
- Policy document
- Renewals
- Assignment



Term assurance

- Pays out a lump sum in the event of death occurring within a specified period
- Premium depend on amount insured; age, sex and family history; health
- Can be level term, decreasing term and increasing term
- Can have option to renew or convert into whole of life

Whole of Life

- Non-profit - guaranteed sum only
- With profits - sum insured; annual bonuses; terminal bonus
- Unit linked - return linked to performance of underlying funds
- Uses - life cover; part of a pension plan or mortgage



Types of Protection Products



Critical illness

- Pay a lump sum in event suffer from a critical illness
- Illnesses covered will be closely defined
- Some significant illnesses may be excluded
- Illness resulting from certain activities, such as war or civil unrest, will not be covered
- Range of conditions need to be met before payment so close examination needed



Income protection cover

- Pay out an income benefit when a person is unable to work
- They run for a set term
- The circumstances under which a benefit will be payable are clearly defined
- They provide a regular income after a certain waiting period
- Payments will differ or cease on return to work



Types of Protection Products



Mortgage Protection

- Cover short term inability to work
- Meet cost of mortgage payments
- Issued on a level basis so regular reviews are needed so that the cover reflects the payments due as mortgage interest rates change
- The amount of benefit payable can be reduced to take account of income from other sources and there may be limits on the maximum amounts that will be paid
- As a result, the amount of benefit paid may not cover the mortgage payments



Personal Accident

- Usually annual policies
- Relatively inexpensive but limitations
- Cover may be the lower of a set amount or a maximum percentage of the individual's gross monthly salary
- Waiting before benefits start may be 30 or 60 days
- Insurance company will assess eligibility at the time of the claim and may refuse a claim as a result of pre-existing medical conditions even if they have been disclosed



Types of Protection Products

Medical Insurance



- Cover the cost of medical and hospital expenses
- May be taken out by individuals, or provided as part of an individual's employment
- The costs that will be covered are usually closely defined.
- There will be limits on what will be paid out per claim, or even over a period such as a year.
- Standard care that can be dealt with by a person's local doctor may not be included.
- Again, there will be exclusions such as for pre-existing conditions

Long Term Care



- Provide funds needed in later life to meet the cost of care.
- Cost of nursing home care is very high
- Need to check amount of state funding for care costs that will be available
- Premiums will be expensive reflecting the cost of care
- Benefit will normally be paid as an income that can be used to cover the expenditure



Main types of business protection

- Key person cover; shareholder protection; partnership protection



Examples of uses

- To provide indemnity cover for claims against the business for faulty work or goods
- To protect loans that have been taken out and secured against an individual's assets
- To provide an income if the owner is unable to work and the business ceases
- To provide payments in the event of a key member of a business dying to cover any impact on its profits
- To provide money in the event of death of a major shareholder or partner so that the remaining shareholders can buy out his share and his estate can distribute the funds to his family



Assessing Protection Products

Factors to be considered when selecting a product

- Price
- Product features
- Charges
- Commission structure
- Tax treatment

Factors to be considered when selecting a product provider

- Financial strength
- Quality of service
- Investment choice and performance

Criteria that solutions should meet

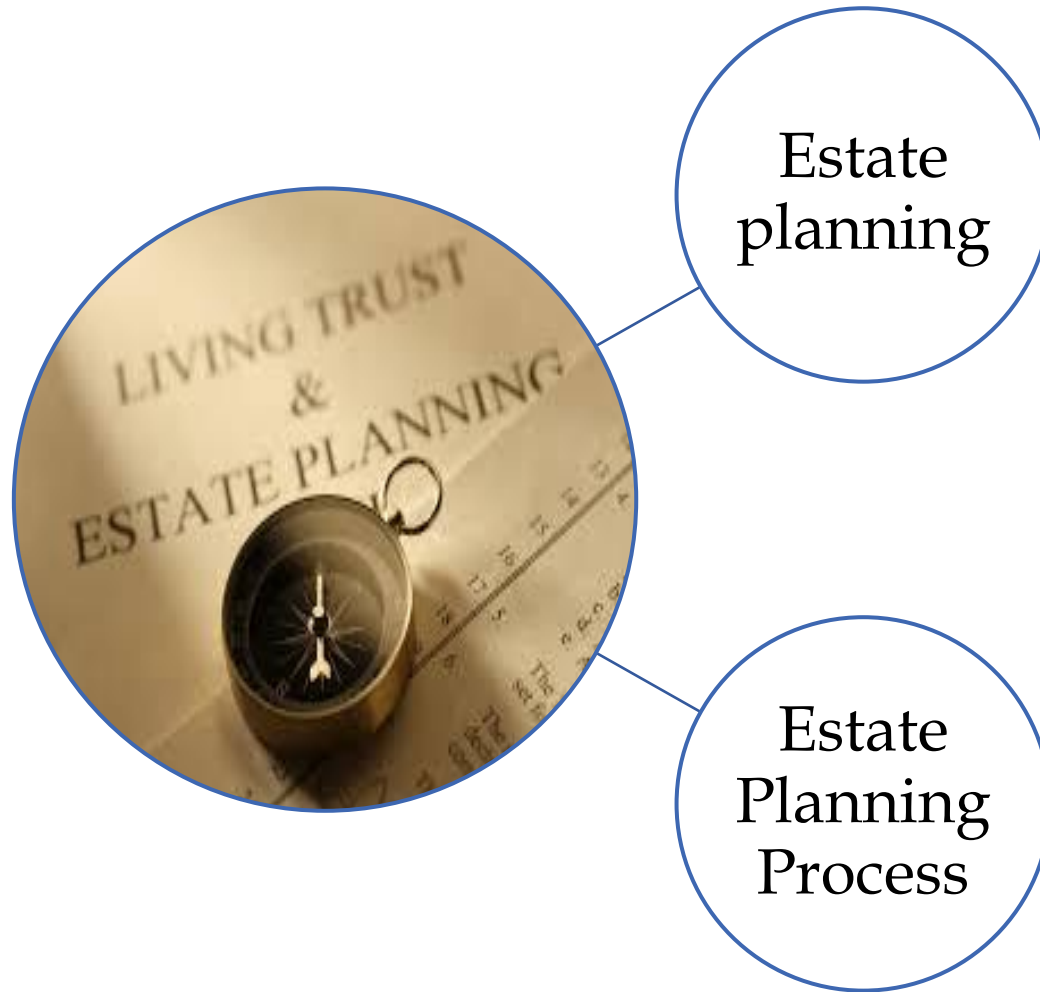
- Must clearly be adequate to meet the client's needs
- Should be consistent with the client's attitude to risk
- Should be as tax-efficient as possible
- Must be affordable to the client and realistic, given their level of disposable income



Content of a Report

- Date of report.
- An introduction that explains the content of the report.
- The current position of the client limited to the most important aspects and a summary of their current protection arrangements.
- The objectives and priorities that have been agreed with the client.
- The recommendations that are being made, how they relate to priorities and objectives and an explanation of the choice of provider.
- Considerations that have been deferred until later.
- Any tax implications of the recommendations on the client's position.
- The action needed to implement the requirements.





- Take appropriate steps to ensure that accumulated wealth passes to their intended beneficiaries and in as tax efficient method as possible
- Steps that can be taken vary but some key stages



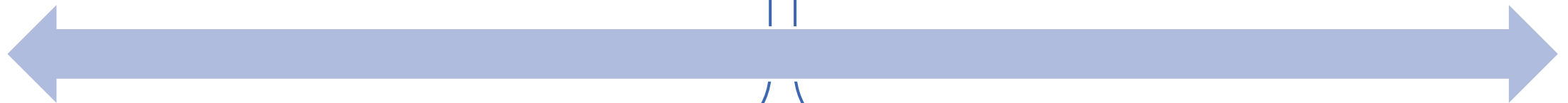


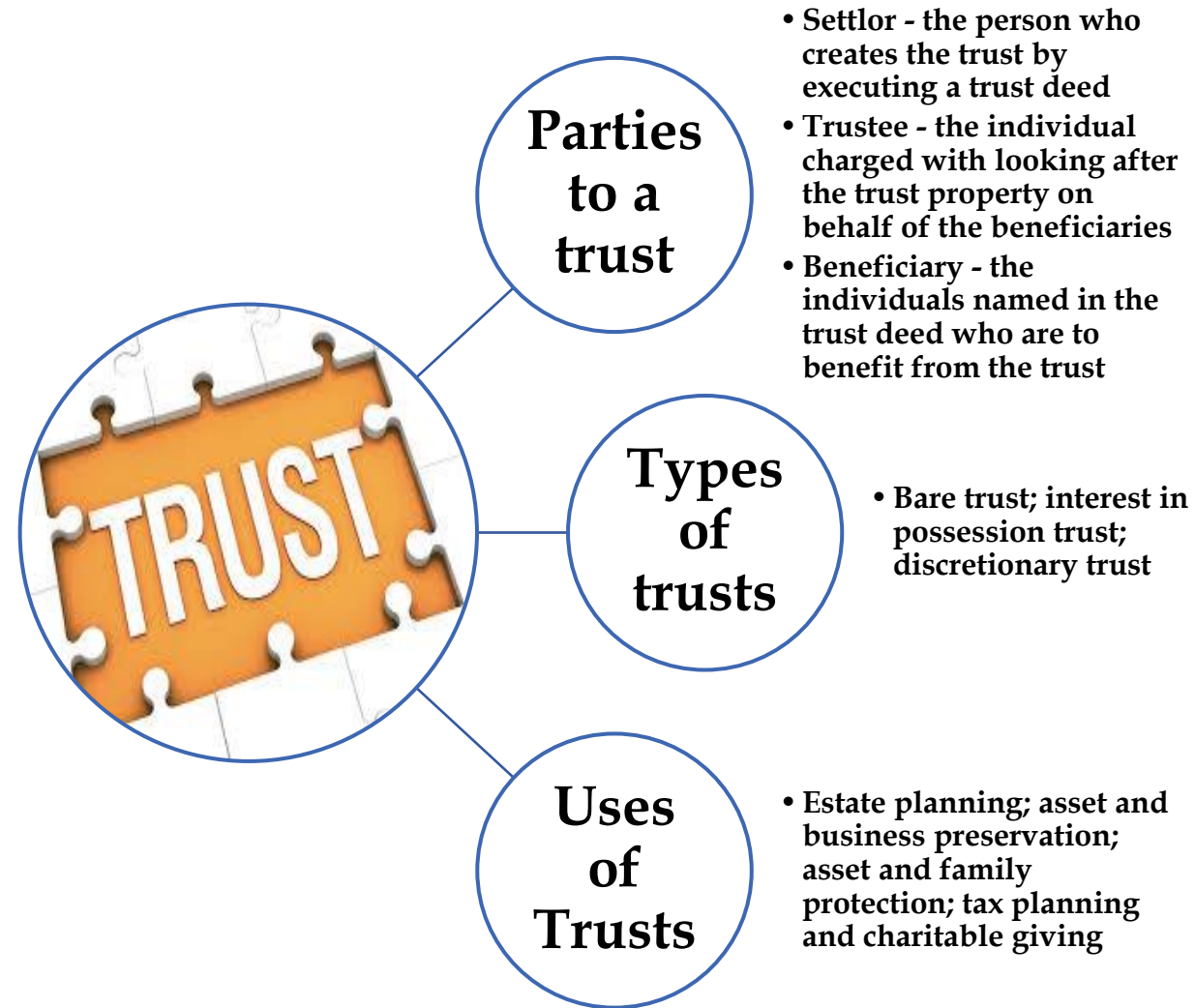
Execution of a Will

- Where possible essential to ensure assets pass in accordance with their wishes
- Specialist advice needed especially if own property overseas
- Inheritance laws will usually determine who receives what if no will
- Where it is not possible to make a will, give consideration to an offshore trust



Inheritance Tax





Offshore Trusts



Offshore asset protection trusts used by wealthy as part of their overall tax planning strategy



Established in offshore financial centres and use discretionary trust structure known as offshore asset protection trust



Uses

- Privacy and protection
- Wealth preservation
- Tax planning - inheritance tax; income tax; capital gains tax
- Legal certainty, flexibility and efficiency



Uses of Foundations

Private

- Alternative to trusts for clients from civil law jurisdictions
- Can be used to achieve the same ends as a private trust and are highly flexible
- May also be a suitable vehicle for asset protection as it divorces the ownership of the assets from the founder.
- Can be used as part of a larger wealth management structure, holding various companies or assets or can hold more high-risk, less income producing assets which may not be appropriate to be held by all trusts.

Charitable

- The term foundation has positive connotations for philanthropic clients.
- Its purposes do not have to be exclusively charitable and so can be more flexible than the traditional charitable trust.



The purpose is to eliminate such businesses that are not in compliance with Shariah principles. These businesses are classified into two:

- Those business organizations whose core business activities are forbidden explicitly in Quran & Sunnah.



Islamic Investment - Financial Screening (E)

- ❑ Under Financial Screening, companies that use too much leverage are excluded from the investment universe.
- ❑ Financial ratios can vary between Shariah Supervisory Boards.
- ❑ The generally accepted financial ratios are as follows:

$$\frac{\text{Conventional Debt}}{\text{Market capitalisation}} < 30\%$$

$$\frac{\text{Total Interest+Income from non-compliant activities)}}{\text{Income}} < 5\%$$

$$\frac{\text{Interest Bearing Deposits}}{\text{Market Capitalization}} < 30\%$$



Financial Planning Matrix

