For intermediaries only

Executive income protection – financial security for your clients

Case study

Meet Dan, a company director aged 40 who has just set up a limited company. Following advice from the company's accountant, the company needs a workplace pension scheme with pension contributions being paid both by Dan and by the company.

A workplace pension scheme is set up where he's making personal contributions and the company is paying employer contributions. Dan would like to try and retire at age 65 with a gross income of £30,000 a year.

Dan also knows that should anything happen to him (accident or illness), and he's unable to work, he has no other income. So he decides to take out income protection to protect this.

Scenario one | Personal income protection (IP)

- Dan is now aged 50, becomes unwell and has to make a claim on his personal IP policy.
- With personal IP, your pension contributions are restricted to a maximum of £2,880 each tax year (£3,600 after tax relief)[1] because the claim payments aren't classed as relevant UK earnings. However, as Dan could only insure a maximum of 62% of his income under his personal IP policy, he can't even afford this, so stops contributing to his pension.
- Dan's personal IP policy doesn't provide cover for the company to continue making employer contributions into Dan's pension.

Consequences

- Dan's protected his income until his retirement age of 65 when his personal IP policy ends.
- At age 65 his claim payments stop.
- But what happens to his income the following month? Instead of potentially retiring with a pension of around £30,000 gross a year, it could be worth much less as he's been unable to contribute to it for the last 15 years.

Summary

- Dan's protected himself **pre-retirement only** and hasn't been able to maintain his retirement savings at the level he'd planned.

[1] This information is based on our understanding of current legislation, taxation law and HM Revenue & Customs (HMRC) practice, which may change.

Scenario two | Executive income protection (IP)

- Dan is now aged 50, becomes unwell and his company has to make a claim on its executive IP policy.
- As the executive IP claim payments are paid to the company, it can use this to continue paying Dan 80% of his monthly salary. As he'll continue to receive a salary, this counts as relevant UK earnings. Dan can contribute up to 100% of his relevant UK earnings to his pension in the current tax year or up to the annual allowance of £40,000, whichever is lower[1]. This means the total sum of any personal contributions, employer contributions and tax relief received, can't exceed the £40,000 annual allowance.
- As Dan is still receiving a salary, he can afford to continue making his regular pension contributions.
- The executive IP policy covers the company's employer pension contributions, so it can continue making employer contributions into Dan's pension.

Consequences

- When Dan reaches age 65 and his claim payments stop, the following month his pension could potentially be the £30,000 gross a year he was hoping for.
- This is because both Dan and the company continued contributing to his workplace pension during the time when he was unwell.

Summary

- Dan's protected his pre-retirement income **and** maintained his and his employer's regular pension contributions – giving himself the best opportunity to achieve his retirement goals.

For help and support with income protection, speak to your usual Aegon sales representative.