Grandparents can make a grandchild a millionaire from just £240 per month

According to data produced by Skandia, if grandparents put just £240 a month (which equates to £300 a month gross contribution) into a pension for a grandchild each year for 18 years, when the grandchild reaches age 60, they could be a millionaire.

This is based on 6.5% investment growth p.a. and no further contributions being made by the child. The child can of course make further contributions when they start work to create an even bigger pension fund.

From the moment a child is born, they are eligible to receive contributions of up to £3,600 into a pension each year. Anyone is able to make the contribution on behalf of the child. Unlike other investment options, such as a junior ISA, a pension can provide basic level tax relief even for a child who is not working, making it an extremely attractive long term savings option. On an annual contribution of £3,600, £2,880 is paid by the grandparent and £720 is paid by the government into the pension in the form of tax relief.

The money is, of course, locked away until the grandchild reaches at least age 55, which might not be considered a bad thing. Children born today are unlikely to enjoy the same level of retirement income funding that the current level of baby boomers are enjoying. They will need to be more self-providing as support from the state is likely to diminish, and arrangements like final salary pension schemes disappear.

The younger generation do not always understand the need to save for retirement, and many cannot afford to. Parents already find themselves needing to put aside for their children's later education. Therefore, opportunities for grandparents to make significant contributions are not to be missed. It is not until someone approaches retirement and they are faced with a finite income until they die, that they wish they had saved more. Those in retirement are best placed to pass this wisdom on to the younger generation, and opening a pension for them is a good way of ensuring their long term financial future.

If grandparents plan to leave some of their estate to their grandchildren and have surplus income from their own pension income, this is an extremely tax efficient way of passing money to them. If the surplus income is available from an income withdrawal arrangement, it will take money out of a 55% death tax charge environment. If the surplus income is created from an annuity payment, the contribution to the grandchild's pension takes the money out of their estate.

Once the contribution is made into the child's pension, the future investment growth of those contributions belongs to the child, creating significant longer term value compared with the money remaining within the grandparent's estate. The income tax paid by the grandparents on the pension income can in part or whole be offset by the income tax relief boost the child receives on the contribution made.