MONEY View

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moneysprite

Your Pensions, Savings, Investments and Protection newsletter from Moneysprite

PENSION Freedom

It's not often that pensions are a topic of conversation around the kitchen table, in the pub, or on a walk!

» The planned reforms from April, however, have got lots of people talking and thinking about pensions.

And it's not just pension planholders coming up to retirement that are considering this issue. It will also impact upon those in the workplace who are looking to build up their pension pot (or thinking about taking one out), recognising that the new rules may require a change in strategy. Furthermore, even those with an annuity may get in on the act, as there has been a suggestion of allowing them the option of cashing it in.

So it's clear that these changes will have an impact right across the board, irrespective of age, lifestyle situation, attitude to risk, and tax position. And whilst it's good to chat about this amongst friends and colleagues, it also makes sense to take professional advice, should you want to find out more. We set out in this issue some of the key developments.

Pension reforms

In short, from 6 April 2015, anyone aged 55 or over will be able to take their entire 'defined contribution' pension fund however they want. This will enable most planholders to draw down as much, or as little of their pension, at anytime.

The first 25% will be tax-free either as one lump sum, or as the first 25% of multiple lump sums. The remaining 75% would be taxed at the person's marginal rate.

Historically, three-quarters of the 320,000 or so that retire each year opted for an annuity, which offers a regular guaranteed income. *(Source: HM Treasury, March 2014)*

For many, an annuity may still be the best route, but it does open up a whole host of choices, such as:

- Take it all out and spend/invest as you wish, whilst being mindful of the tax issues.
- Take a lump sum, or a series of them.
- Enter a flexi-access drawdown plan.
- Buy an annuity from the pension scheme provider or via the Open Market Option.

With drawdown and annuities there are already new options and, no doubt, more will be introduced as the industry gets to grips with this brave new world.

Taxation at death

Whilst pensions that were still invested could be passed on at death under the old rules, a sizeable 55% tax was applied. With the changes, the retirement pot of someone who dies before the age of 75 will no longer be taxed when passed on. Similar rules now apply to annuities (joint life or an annuity with a guaranteed term).

And a pension pot passed on after the age of 75 may be taxed at 45% for a lump sum payout or at the beneficiary's marginal rate if taken as income. From 2016/17 it may all be at the marginal rate (the exact details still need to be confirmed). Again annuities are likely to be treated similarly.

Choices ahead

In this issue we take a broad look at annuities and drawdown, alongside other options should you want to get hold of some (or all) of your money. And this is why options such as buy-to-let, paying off debts, home improvements or gifting money to family members may also come into the mix.

Whatever you opt for, it's essential that you take advice before you act.

HM Revenue & Customs practice and the law relating to taxation are complex and subject to individual circumstances and changes which cannot be foreseen.

Welcome....

to this newsletter, which covers some of the key financial issues of the moment.

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YOUR journey ahead...

The general message from the chancellor when introducing the pension reforms was that people who have worked hard and saved all their lives should be free to choose what they do with their money.

» The new freedoms could mean that some people remain invested in their existing pension plan and draw an income from that. This is called an Uncrystallised Funds Pension Lump Sum (UFPLS). These funds are 'uncrystallised', as they have not yet been used to pay a scheme pension, buy an annuity, or designated to a flexi-access drawdown fund. There are numerous rules applicable to them, so talk to us to find out more.

Annuities

The Financial Conduct Authority (FCA) recently investigated the annuity industry. It was concerned that too many pension planholders (60%) had opted for the plan offered by their scheme provider, or its third-party tie-up, rather than shopping around to see what else was on offer. The FCA believe that over three-quarters of them could have received more from elsewhere.

And as part of that process, called the Open Market Option, the FCA felt that an even greater number would have done better (nine out of ten) if they qualified for an **enhanced annuity.**

This is where the payout could be substantially more if a person suffered from a specific health or lifestyle issue such as diabetes, cancer, a heart condition, or from being a smoker.

The rationale behind the higher payout is that they're not expected to live as long. It's then down to them to beat the odds!

Overall, the FCA suggested that: *'for people with average-sized pension pots, the right annuity purchased on the open market offers good value for money relative to alternative drawdown strategies and may therefore be a good option for those with low risk appetites'.*

(Source: FCA, Annuities sales practices, December 2014)

But, with an annuity there's generally no going back once you've chosen this option, albeit new rules have been introduced to make them more flexible.

Drawdown

At the other end of the scale are **drawdown** products, which could potentially offer a better return but do come with a higher degree of risk, as you'll still be investing in the stock markets, etc.

This product is not suitable for everybody and has historically been more appropriate to those who have sizeable pension pots, and are less averse to risk.

However, from April, this sector will also expand with the introduction of **flexi-access drawdown funds** which will be the format for all new drawdown plans from that date. These are designed to cater for more needs on the risk scale and fund size; with the existing restrictive rules affecting how much you can take out, being swept away.

And the change in the tax rules means that you won't be limited to just one chance to take up to a quarter of your pension pot as a tax-free lump sum. Alternatively, you can make as many withdrawals as you want and each time 25% of it will be tax-free. Although you have to be mindful of balancing the easy access to cash, with your investment strategy, and possible future tax bill for the other 75%.

Drawdown planholders who took out their plan prior to 6 April 2015 can also enjoy these freedoms, if wanted, by converting to flexi-access.

It's quite likely that the rules will be tinkered with, and providers will continue to develop their offerings, so do make sure you talk to us.

These changes affect those with **defined contribution pensions,** who need to turn their retirement pot into an income themselves - unlike those with **final salary or defined benefit pensions** who get a set income provided for them.
Whilst you may be able to switch from a final salary scheme to enjoy the new freedoms, in most circumstances, it's unlikely to be the best move.

Cashing in an Annuity?

First off, this may never materialise, as at this stage it's an idea that has been proposed by the 'current' Pensions Minister, Steve Webb - and with the Election looming, who knows who will be in charge after 7 May.

Most annuities are designed to be a lock-in lifetime commitment which, in turn, promise to deliver a guaranteed income for life. The initial response when the 'cash in' idea was raised, was that it was 'unworkable', but more recently it's generated positive interest from some of the life companies.

If this option does materialise and it's of interest, then it's vital that you take advice, as the most suitable solution could simply be to stay with what you've got.

INVESTMENT Considerations

Plenty of issues to assess in 2015.

» Britain faces years of steeper public borrowing, slower debt reduction and higher taxes after May's election, despite the economic recovery remaining on track, according to the *Financial Times*' annual survey of economists.

For 2015, they expect the 'decent' recovery to continue, even if expansion slows slightly. With the general view that whoever is in power from May, the new government is unlikely to stick with plans for deep spending cuts to reduce the deficit.

And as for the impact on mortgages, not a single economist out of the 85 who expressed a view, thought that the Bank Rate would rise before the Summer, and a large number felt that the rate rise would be held back until at least November.

(Source: Financial Times, Annual Economists Survey, January 2015)

Your investment strategy

To some extent the economic outlook may help shape your investment approach. Everyone, though, will have different objectives, which are also dictated by **life stage, attitude to risk, available funds** and **tax position.**

For most investors, it's sensible to spread the investment net in order to deliver measured growth. And, in most cases, to play the longer-game, rather than chasing potential short-term fluctuations here and there.

Broadly, if you were to consider four key asset classes: **equities, property, fixed interest** (such as government and corporate bonds) and **cash** - it's equities that are likely to deliver the greatest level of risk (and potential reward). If you are working to a long timeframe, where you're not immediately dependent on the money - you may decide that this should form the bulk of your investment portfolio.

The general rule has been to move into less risky investments the closer you get to retirement - as you may have too little time to make up any shortfalls, should events turn against you. This could still be the best tactic, but with less emphasis now being placed on taking up an annuity at retirement (as a result of the pension reforms), alternative strategies may also need to be considered.

Be tax-efficient

It makes sense to take advantage of the tax-efficient schemes that are on offer. For example:

Pensions - With the abolishment of the 55% 'death tax', putting surplus cash into a pension could become more attractive as a way to help reduce inheritance tax (IHT) bills, with IHT payable at 40% above the £325,000 threshold. Added to this are the tax benefits when paying into a pension, with every 80p a standard rate taxpayer pays in, the government adds 20p, effectively delivering a 25% uplift in the contribution. The situation is even better if you're a higher rate taxpayer! And should your employer have an Additional Voluntary Contribution scheme (where they may also contribute), you could benefit further.

Individual Savings Accounts (ISAs) - Did you know that if you used all of your ISA allowances since it was launched in 1999, it would have added up to over £136,000 of investments, and any growth on that amount would be sheltered from tax?

The value of investments and the income from them can go down as well as up and you may not get back the amount originally invested.

HM Revenue & Customs practice and the law relating to taxation are complex and subject to individual circumstances and changes which cannot be foreseen

Do get in touch if you want to talk further about your pension and investment objectives and take a look at the story below to find out the latest about ISAs.

ISA news

» Millions of Individual Savings Account (ISA) holders were given a boost when the chancellor abolished the 'death tax'. ISAs can now be passed on to a spouse, or civil partner tax-free. Previously the ISA tax 'wrapper' passed away with its owner, and the money that had been sheltered became liable for income and capital gains tax.

According to HM Revenue & Customs, 150,000 married ISA savers die each year, and the tax advantages died with them.

But from 6 April 2015, the surviving partner will be able to invest as much into their own ISA as their spouse used to have, on top of their usual allowance.

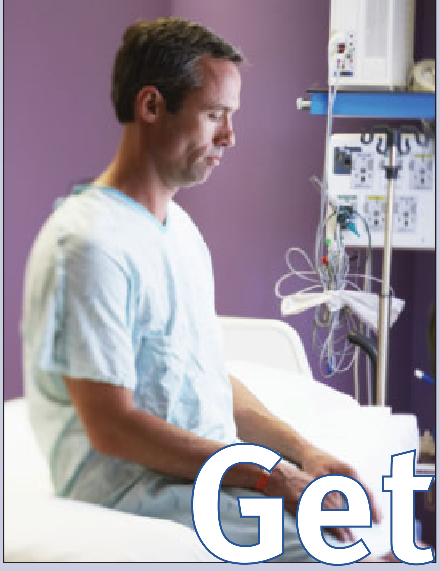
Improved limits and flexibility

With an ISA any interest, income or growth you receive will be free from any personal liability to income or capital gains tax. For the 2014/15 tax year the individual limit was increased to £15,000, a £3,480 rise over the previous year, and for 2015/16 it is £15,240.

And savers have total flexibility to save or invest as they wish, up to these thresholds - in 'cash', or 'stocks and shares', or any combination of the two.

Let us know if you have any questions, or would like to hear more about ISAs.

A stocks and shares ISA is a medium to long-term investment, which aims to increase the value of the money you invest for growth or income or both.



1 in 10 of us will face a period of sickness absence of more than 6 months during our working lives. Whilst you may have life cover in place, how would you (or the family) cope if a wage earner was off work for a long period of time?

(Source: Demos survey, April 2013)

Get PROTECTED

» Taking out protection cover can often be viewed as an unnecessary expense - until you compare the cost of 'having it and not needing it' vs. 'needing it and not having it'!

But if you had a critical illness such as a heart attack, a serious back injury, or suffered from stress, then the last thing you'd want to do, is rush back to work to ensure there's an income coming in.

Of course, if you're an employee there might be the buffer of a period of cover as an employee benefit. After that, you may be able to fall back on state benefits of limited value. Understandably, you are more vulnerable if you're self-employed.

So it makes sense to protect yourself. In the process, you'll need to work out the sum required to ensure that you don't over-insure (and pay a higher premium), but secure enough cover so that you can focus all your energies on recovery.

There are two products that can possibly meet this need. Both may be suitable for you, or simply opt for the one you think is most relevant.

Critical Illness

A Critical Illness policy will cover a wide range of serious illnesses (although not all forms of cancer and heart disease may be covered). It can be taken as a stand-alone policy, or as a bolt-on to a life assurance plan, and policies may vary with regard to the illnesses covered. If you're able to claim (91.8% of claims are met), then you'll get a lump-sum, with the latest annual data showing an average payout of around £60,000.

Income Protection

This is a long-term insurance policy that's designed to pay out a tax-free monthly sum in the event that you're unable to work due to illness or injury. The policy pays out once a pre-agreed period has passed, generally ranging from one to 12 months after you put in a claim. The longer the 'deferral' period, the lower the premium. And it pays out until you can start working again, or, in some cases, until you retire.

And do be realistic about how much you think you might require until you're able to return to work, or have retired. As it may not need to be life-changing.

A degree of realism is reflected by an average claim of around £11,500, with a 91.1% success rate for claimants.

(Source: Association of British Insurers, 2013 figures, released May 2014)

The choice for you

As you can see these products largely cover different areas and address differing circumstances, although there will be some degree of crossover.

Do have a chat with us so that we can run through the options and give you a feel for what it may cost to deliver cover for your needs. In the meantime, have a look at the chart to the right as you may be surprised how easily you could find some or all of the premium required.

How to afford the extra protection cover

You might feel you're already stretched to the limit to find the money to pay for protection.

However, it may be easier than you think when you consider all those little items we may take for granted, like the odd drink or a magazine. In fact, you might be surprised to find out how quickly it all adds up.

Treats	£ Cost/unit (est.)
Soft drink	1.00
Snack	1.00
Magazine	1.75
Coffee	2.50
Pint of beer or lager	3.50
Glass of wine (175ml)	3.50
Taxi	5.00
Cigarettes (pack of 20)	7.00
Take-away meal	7.00
Total =	**£32.25**

For example, if you **cut out just one unit each week** of the above items, then you could **save around £140** across a month. And, in many cases, that'll be more than you need to cover the cost of your protection policy.

We don't expect you to give up all of life's little luxuries. But, by keeping an eye on your spending, you could afford to set aside a little extra to improve your financial security.

As with all insurance policies, terms, conditions and exclusions will apply.

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