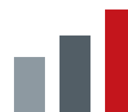
MONEY view

Spring 2015



NORRIS & FISHER
INDEPENDENT FINANCIAL PLANNERS

Your Pensions, Savings, Investments and Protection newsletter from Norris & Fisher Independent Financial Services Ltd

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 issues of the moment that may affect your financial wealth.

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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.

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.

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.

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.

If you're looking for additional funds and are a homeowner, aged 55+, then do consider...

Equity RELEASE

» With all the new freedoms being introduced from April, don't lose sight of another option - your own home.

The average UK house price has risen by 6.8% over the last year and now stands at around £188,500 (surpassing the 2007 peak), which means that many homeowners could be sitting on a sizeable investment.

(Source: Nationwide House Prices, January 2015)

This is an issue that's reinforced by a survey from LV=, an equity release provider. In its annual *HIPpies 'home is pension'* report, 60% of 50+ homeowners (up from 44% in 2013) are planning, or considering, using money locked in their property to fund their retirement through options such as downsizing, equity release, or moving to a less expensive area.

(Source: LV= HIPpies 'home is pension' survey, Sept. 2014)

A key influence over any decision is that many will have an emotional attachment to their home, and perhaps be keen to remain close to family, friends and local amenities. In this scenario, staying put may be the preferred option.

If that's the case, then **Equity Release** could be a route, if certain criteria, such as being aged over 55 are met. With record lending figures in 2014, and an annual growth of 29%, equity release is now proving to be a popular route for many.*

The options

There are two main types of equity release plans - you can either borrow money, which is secured against your home (Lifetime Mortgages), or sell part, or all of your home (Home Reversion schemes). The former accounts for the vast majority of plans taken out.

Most plans start at about £10,000 and, on average, around £65,000 is raised.*

However, before you proceed with an equity release plan, there are a number of issues to consider to ensure that it's the most suitable route for your needs (and perhaps those of your family too).

Lifetime Mortgages

This is similar in principle to a standard mortgage, with the main difference being that with most schemes there are no monthly repayments to make and the loan (and accumulated interest) is redeemed when you, or the final planholder dies, or moves into long-term care.

The most popular route is to opt for drawdown, where instead of taking a lump sum at the outset, drawdown allows you to take what you need within certain agreed amounts and time constraints.

The effect of this is that it may enable you to stay within limits for means-tested benefits. It will also lessen the impact of the 'rolling-up' of the interest that's not being paid on the loan, as there's no point paying interest on money you don't need at that moment in time.

To gauge the impact of roll-up, if the rate of the lifetime mortgage loan is 6%, for example, a £50,000 loan taken at outset (with the accumulated interest) would have doubled to around £100,000 after 12 years. Although, against this you may need to consider if house prices might work in your favour across the same timeframe, and also some schemes do allow monthly payment of the interest.

Safeguards for the planholder

The Equity Release Council is the industry trade body, of which its lender members represent over 90% of all equity release lending. It has a number of rules in place to help safeguard the needs of borrowers, such as:

- **No debt left for the dependents.**
- **You will never lose your home.**
- **You can still move elsewhere** (although you may have to repay part of the loan, if moving to a cheaper property).
- **The planholder can remain in the property for life** (or until the final planholder moves into long-term care, provided the property remains the main residence).

*(Source: *Equity Release Council, 2014 figures)*

For Equity Release, we are introducers,, once we have established if this is a reasonable option for you.

These are Lifetime Mortgages and Home Reversion plans. To understand the features and risks, ask for a personalised illustration.

Lifetime Mortgages and Home Reversion Plans are the two main types of Equity Release.

An Equity Release plan will reduce the value of your estate and as a result there may be no value left to pass on.

Equity Release will not be suitable for everyone and may affect your entitlement to State benefits.

As Equity Release is a complex area only specially qualified advisers can give advice on these schemes.

■ The contents of this newsletter are believed to be correct at the date of publication (February 2015).

■ Every care is taken that the information in *Money View* is accurate at the time of going to press. However, all information and figures are subject to change and you should always make enquiries and check details and, where necessary, seek legal advice before entering into any transaction.

■ The information in this newsletter is of a general nature and does not constitute advice. You should seek professional advice tailored to your needs and circumstances before making any decisions.

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