What the Papers Say

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This is the latest in a regular series of summaries where we look to review some of the main articles written in the financial sections of the Sunday papers.

These articles often cover issues that are important to our personal financial well-being and we hope that the summaries will provide you with information and ideas that will be of interest to you.

If you would like to discuss any of the issues raised within these summaries or any other financial planning issue, please do contact our wealth management division on 01204 414243.

Articles reviewed

"I plan to switch from Child Trust Funds to Junior ISAs"

The Mail on Sunday

"Five scenarios where annuities are still the best bet"

The Sunday Telegraph

"Pension Freedoms – Use your pension to cut your inheritance tax bill to zero"

The Telegraph (5th April 2015)

With effect from 6th April, parents of children born between September 2002 and January 2011 who were given a voucher by the Government to set up a cash or investment fund for their children in a Child Trust Fund now have the option of transferring to a Junior ISA.

Low income families were given £500 while other families received £250 originally but the scheme was scrapped for new savers in 2011 and replaced with equally tax-efficient Junior ISAs but with no free cash. Both schemes allow parents to invest for their children within a tax-free wrapper similar to an adult ISA but with a lower annual limit.

Previously those who had a Child Trust Fund could not open a Junior ISA, but with the newer schemes in place, providers of Child Trust Funds dropped off and choice became restrictive in comparison. Child Trust Funds are now considered the poor relation to Junior ISAs with fewer investment options, higher charges and lower returns on cash accounts according to Chase de Vere.

As an example, Coventry and Nationwide building societies pay 3.25% gross interest on a Junior ISA whilst the highest rate on a Child Trust fund is 3% from Yorkshire Building Society, but 0.70% is a bonus lasting just 12 months. The next best rate is 2.65% from Skipton Building Society.

In 2015/16 parents can save £4,080 a year for children under age 18 living in the UK. There are two forms of Junior ISA, cash and stocks & shares. The monies are invested in a tax efficient environment where no tax is due on the interest received on cash, or on any capital growth / dividends received. Children can have one or both types of Junior ISA. The child can take control of the account when they are 16 but cannot withdraw the monies until they turn 18.

Before transferring a Child Trust Fund to a Junior ISA you should consider the following:

- **Charges** – many Child Trust Funds are classed as "Stakeholder Accounts" meaning that charges are capped at 1.5% and investments are spread between a range of assets including less volatile bonds and Government Debt as well as shares. There isn't an equivalent Junior ISA. As an example, the L&G UK Index Fund will charge 1.5% in a Child Trust Fund, but the same fund through a Junior ISA could cost on 0.56%, other index tracker funds carry even lower charges through a Junior ISA.
- **Diversification** – parents should ensure that their children's savings are appropriately diversified. The oldest children with original plans are 13 meaning action may be needed to reduce risk or change the investment profile.
- **Transfers** – not all Junior ISAs will accept a transfer in from another provider.

Should you wish to review your Child Trust Funds to see whether it would be appropriate to transfer, please contact us. We can help you track down your accounts, review the market for an appropriate solution and compare charges and investment choices.

“Five scenarios where annuities are still the best bet” “

The Sunday Telegraph

Annuities are widely derided as an outright rip-off as a result of poor rates, but only an annuity can provide the certainty of an income for life. Knowing you have a guaranteed income for the rest of your life can still be a good thing that many people will value. If you are interested in buying an annuity, there are several things you can do to improve the rate you achieve and the income for the rest of your life:

1. **Delay your purchase** – the average age people purchase an annuity is 65, given that life expectancy has increased, the term of income payments can span 25 years or more. This reduces the overall rate of income, whereas if you defer to 75 your annuity may have to last 15 years which is 40% less and naturally you'll get a lot more each year.

2. **Get an “enhanced” annuity** – if you have a health condition that will typically mean a lower life expectancy, insurers reflect this by offering higher rates. Shopping around for these types of annuities is essential as the differentials between providers can be huge depending on the medical condition.

3. **Check whether you have a “super pension”** – some older pensions included a perk, the “guaranteed annuity rate” which can be double those normally available, has turned out to be very valuable. With these policies, it's vital not to switch until you have considered all options including the guaranteed rate. There can be some restrictions on the way the pension income needs to be taken however it is important to seek advice. If you have several pensions the best route could be to secure the guaranteed rate with these types of policies first before considering other options with the remaining pension funds. It may also be worthwhile not taking the 25% tax-free lump sum and use the money to buy more annuity income at an unbeatable rate instead.

4. **Defer the State Pension and use your private one instead** – this relies on deferring the state pension for a year which results in a 10.4% increase in the payment. You could bridge the gap with your private pension. When you do then start taking it, the extra income is roughly twice what you would have received had you used the monies in your pension to buy an annuity instead. This option is only of benefit to those who reach their state pension age before April 2016 when the new single-tier state pension is introduced.

5. **“A cheaper way to get annual increases”** – final salary pension schemes include annual increases in line with the cost of living. This option can be expensive within an annuity environment, as an example the income from an index linked annuity can be almost half that of a level annuity. This has led to many taking level annuities which now have no protection against inflation. For those who have purchased an inflation linked annuity, with inflation at an all-time low, this could prove very costly. Another option is a fixed rate of increase i.e. 3% where the starting income is still lower than a level annuity, but higher than an inflation linked annuity. There is also the option of an investment-linked annuity which aims to benefit from long-term growth in the stock market.

With any retirement strategy it is important to consider all options, a combination of annuities both level and/or investment linked alongside more flexible routes should be considered. Securing a guaranteed income to cover your essential expenditure through an annuity with other retirement options could prove the most appropriate.

Although more flexible options are now available, it still important to consider all avenues before making a final decision.

Pension Freedoms – Use your pension to cut your inheritance tax bill to zero –

The Telegraph (5th April 2015)

With the new “pension freedoms” there are implications around how to arrange your assets to minimise the tax you pay both during your lifetime and even after death. The changes also bring significant opportunities to limit inheritance tax.

In six straightforward steps, you are able to use the new pension rules to avoid death taxes. One of the “hidden” rules within the changes is the ability to pass on pension assets outside a savers estate for inheritance tax purposes. At a stroke, pensions can offer wealthier investors a sudden and significant way to avoid legitimately inheritance tax.

This is a complex area of financial planning, but by following six steps you are able to limit the impact of death duties by simply rearranging your assets.

Step 1, put as much into your pension as you can, while you can. You are limited to an annual contribution of 100% of your pensionable earnings up to £40,000 whichever is lower. But you are able to roll several years allowances together in one year. There are also income tax savings to be made on making pension contributions in comparison to other investment vehicles.

Step 2, be careful not to exceed the lifetime allowance which is currently £1.25m in 2015/16. For example, a 50 year old with a pension valued at £500,000 and no further contributions with investment growth of 6% per annum would have a fund valued at £2.1m at age 75. For some the extra tax charge could be an acceptable price to pay for the tax-free uplift in the pension and the ability to pass on the pension pot to their beneficiaries.

Step 3, ensure you have enough outside of the pension to provide income in retirement. When you die you want to minimise non-pension assets above the £650,000 inheritance tax threshold. The aim of this strategy is to leave your pension intact to pass through the generations whilst you live on other potentially taxable assets.

Step 4, consider giving away assets to reduce your inheritance tax bill further. There are a number of annual exemptions you can use, the use of trusts and other forms of inheritance tax planning can also be used.

Step 5, if you do not wish to give away assets you can consider other "inheritance tax-proof" investments. Investing in AIM listed shares and other business related investments are free of inheritance tax. These investments tend to be higher-risk which is one of reasons they attract inheritance tax relief. You could end up losing more than the inheritance tax bill itself and so this is an area for which specialist advice is needed.

Step 6, write a careful will. Pension assets will be distributed by the trustees of the pension scheme. It is important to provide a letter of wishes to relevant parties which should be revised frequently. There are a number of options available in terms of the distribution of your pension assets on your death: use of an individual trust, a generic trust or under nomination. The route taken has consequences and so it is now important to review your how pension has been set up in this respect. A carefully drafted will is also vital.

Pension Freedoms – Pitfalls

Despite the opportunities, there are plenty of chances to make costly mistakes therefore:

- Don't feel that you have to do something right away. Many pension firms have already admitted that they are being stretched to breaking point by the increase in demand from pensioners.
- Don't land yourself a huge, unnecessary tax bill. Someone with an income of £20,000 wanting to encash a pension fund worth £30,000 would end up paying £4,553 in tax on their pension, some of which would be at the higher rate of 40% if they took it all in one go. Whilst you are able to draw 25% tax-free, the remainder will be added to all other income which could increase your overall income tax liability.
- Don't leave yourself vulnerable to being poor in later life. Underestimating your lifespan can be a problem as can depleting your fund too quickly. Your pension savings could have to last you a lot longer than you anticipate, therefore more sustainable withdrawals could be more appropriate than releasing the fund in one go.
- Don't pay too much for your pension arrangements. The charges which apply to pension arrangements vary between providers with some at a fixed monetary fee and others at a percentage of the fund, both can be costly depending on the size of your retirement fund. It is therefore important to consider the type of pension arrangement you have to ensure that it is appropriate and suitable for you.
- Don't overlook all the pension options, including an annuity. Annuities have had a lot of bad press in the past, but as the article above highlights, they are still an option for some to consider.
- Don't hand your money to fraudsters. Fears have been mounting that sales of inappropriate investments will rocket from April and many have already been mis-sold unregulated investments worth billions. It is important to be vigilant against potential scammers, never talk to cold callers or give away personal information over the phone. Be aware of investments which sound too good to be true, be alert to anyone who encourages you to withdraw money from your pension. It is easier to take money out of your pension than to put it in. Once the cash is out, it is more likely to attract tax.

As with all investments it is important to note that the value of investments and any income taken from them can fall as well as rise. You may not get back the full amount of your original investment.

Any questions?

If you have any questions on any of the articles covered in this publication or would like our help with any financial planning issue, please contact:



Matthew Bromley
matthew.bromley@cowgills.co.uk

Chris Harrington
chris.harrington@cowgills.co.uk

Phil Hart
phil.hart@cowgills.co.uk

COWGILL HOLLOWAY
WEALTH MANAGEMENT (UK) LTD