Whiting & Partners Wealth Management Ltd

Autumn 2017

Bulletin

Setting sail on pensions transfers?

Thousands of people are transferring out of final salary pensions in order to get their hands on a potentially significant cash fund. Once the decision is made, however, it can't be reversed, so it is crucial to make sure you get the right advice.

As much as £50 billion has been taken out of final salary pension schemes since April 2015. Over 80,000 people have transferred out of these defined benefit (DB) pensions in the last year alone according to The Pensions Regulator, swapping a guaranteed inflation-linked lifetime income in return for a cash lump sum.

Rising 'transfer values' are encouraging the trend. A transfer value is the amount of money you receive to put into another type of scheme if you leave your employer's DB pension. These values have increased by up to a quarter in the last year because of falling government bond yields, and they can now be as much as 30 to 40 times the value of the annual pension being given up.

Should you stay or should you go?

Given the size of these transfer values, it is not hard to see why those aged 55 and over might be tempted to take this cash and either spend it or invest it in another type of pension arrangement. Many people may be hoping to pay off debts or leave surplus funds to their children, which is unlikely to be permitted with a DB pension.

You have to weigh this, however, against the security of receiving a guaranteed, inflation-linked income for life, which should also pay a widow (or widower's) pension. The danger for those who transfer out of a DB pension is that they could outlive their savings. The money could run out before they die if investment returns are poor, the funds are not managed effectively, or they spend too much or live longer than expected.

The importance of advice

It is vital to take advice before making any decision. In fact, it is mandatory to do so if the transfer value is more than £30,000. The regulator is now consulting on whether the way advice is given could be improved, to ensure people fully understand the long-term implications of this decision. Remember that once you've taken money out of a DB pension you don't have the option to move it back at a later date.

Occupational pension schemes are regulated by The Pensions Regulator.

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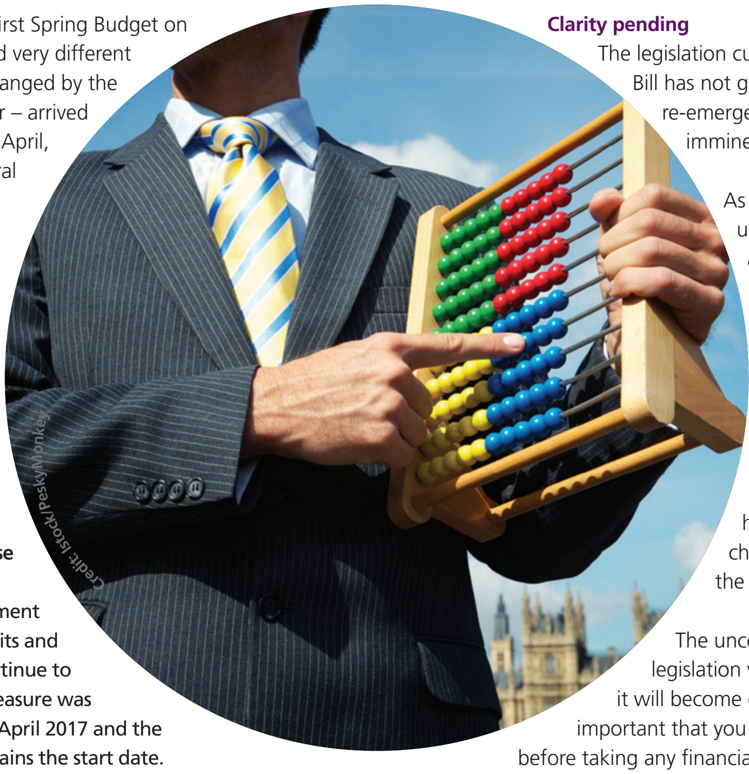
Whiting & Partners Wealth Management Ltd is authorised & regulated by the Financial Conduct Authority.

Elections, Budgets and Bills – what's next?

The events of the first half of the year have left many Budget tax measures in limbo.



When Philip Hammond delivered his first Spring Budget on 8 March, the UK political world looked very different from how it looks today. It had not changed by the time the Finance Bill – the longest ever – arrived 12 days after his speech. Then, on 18 April, Theresa May announced a snap general election and with that predictability started to disappear.

One of the first victims was the Chancellor's super-sized Finance Bill. There was no way the Bill could be squeezed through parliament in the time available before Westminster shut down, so about 80% of it was dropped. Among the measures which disappeared were:

- The reduction in the **money purchase annual allowance** from £10,000 to £4,000. This could affect your retirement planning if you draw pension benefits and also you (and/or your employer) continue to make pension contributions. The measure was originally due to take effect from 6 April 2017 and the government has confirmed this remains the start date.
- The cut in the **dividend allowance** from £5,000 to £2,000, which is still likely to start from next tax year (2018/19). If you are a higher rate taxpayer, this could cost you nearly £1,000 in extra tax on your dividends.

Clarity pending

The legislation culled from the original Finance Bill has not gone away, however, and will re-emerge in a new Finance Bill, expected imminently.

As if that were not enough uncertainty, the Chancellor has also confirmed his original schedule of an Autumn Budget. This marks a shift from the previous pattern of Spring Budgets and Autumn Statements and means another Finance Bill should follow late in the year. The Autumn Budget should give the first indication of how government tax policy has changed – if at all – in response to the election result.

The uncertainty about what tax legislation will be introduced and when it will become effective makes it all the more important that you ask for our updated advice before taking any financial action. It could also mean that the only sensible advice we can give in some areas is 'wait and see'.

The value of tax reliefs depends on your individual circumstances. Tax laws can change. The Financial Conduct Authority does not regulate tax advice.

Are you covered on personal lending?

The boom in personal lending is worrying the Bank of England.

The rate at which people are taking out loans, maximising store credit cards and signing up for car finance is of increasing concern. A recent meeting of the Bank of England's Financial Policy Committee warned that lending is growing rapidly, potentially posing a risk to the UK's financial stability, and to households' own financial wellbeing.

A large number of loans, mortgages and contingent liabilities are not covered by insurance, but they should be. Are *all* your borrowings covered?

Mortgages may be uncovered

Half of UK mortgage holders have no life insurance protection in place, according to a 2016 study by Scottish Widows. These statistics are remarkable. Mortgages are generally people's largest liability. If the main earner in a household dies, the surviving partner might find it impossible to keep making the mortgage repayments. That could mean having to sell the property to move into rented accommodation at a particularly difficult time.

Other loans and credit cards

If you have taken out a loan to buy a car or for some other purpose, it might be covered by payment protection insurance that would pay out if you were ill or lost your job. Check whether you have such cover and what it includes. If it is not your habit to clear credit card balances each month then you should ask what will happen to any uncovered balance if you should become ill or die.

Contingent liabilities and business debts

You should not forget those unseen liabilities that may occur. For example, what if you are a guarantor for a family member's mortgage and they lose their job or their business fails? If you are self-employed then you will also need to remember your business debts.

What type of protection do you require?

The objective is to make sure that your partner and children especially, but possibly other family members, are not left to deal with your debts if you should die suddenly or suffer from a life-threatening illness.

This is easily dealt with by simple 'term insurance'. Term insurance is not necessarily expensive and can often be put in force without a medical examination. The cost of such cover naturally increases with age, so the sooner you are able to discuss your protection requirements with us the better.

Your home may be repossessed if you do not keep up repayments on a mortgage or other loans secured on it. Think carefully before securing other debts against your home.

In June 2017, a leading provider of indices for emerging markets announced that from next year it would start to include shares listed in China in its indices. The decision followed rejections at review in the three previous years and was seen as a major turning point for investment in China. If you would like to review your investment arrangements, please talk to us about your options.

The value of your investment can go down as well as up and you may not get back the full amount you invested. Past performance is not a reliable indicator of future performance. Investing in shares should be regarded as a long term investment and should fit with your overall attitude to risk and financial circumstances.

Inheritance tax receipts hit a new high

Inheritance tax (IHT) is raising more than ever according to HM Revenue & Customs. How much do you want to contribute?

IHT receipts broke through the £5 billion barrier for the first time in the 12 months to May 2017. In April and May 2017 alone, receipts were up over a third on the previous year.

The record tax take is due to three main factors:

1. The nil rate band (NRB) has been frozen at £325,000 since April 2009.
2. Estate values have been rising, thanks to increasing share and property prices.
3. The tax rate above the nil rate band remains at 40%.

IHT tax payments will continue to grow, according to the Office for Budget Responsibility projections – with £6.2 billion of tax expected to be paid in 2021/22.

Mitigation options

There is little chance that any fresh legislation to dilute IHT's impact will appear any time soon, but two measures do offer some scope for mitigating the impact of IHT:

- **The residence nil rate band (RNRB)**, the first phase of which came into force in April this year at a level of £100,000 for each individual. The RNRB will ultimately mean that from April 2020 a married couple (or civil partners) *may* be able to pass on a joint estate of up to £1 million with no IHT payable.

- **Pension death benefits** were granted highly favourable IHT treatment as part of the 2015 pensions flexibility reforms. Lump sum and survivor's pension benefits payable on death are normally free of IHT, although the beneficiary will be subject to an income tax charge if death occurs on or after age 75.

If you do not want your estate's beneficiaries to suffer from that increasing IHT tax take, the sooner you start planning the better. If you have already undertaken some planning, then you might well need to review matters in the light of the RNRB and pension rules mentioned above.

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When you've used your ISA allowance

With the Individual Savings Account (ISA) allowance now at £20,000, it's difficult for many people to save more than that amount each year.

However, where unexpected or additional money becomes available, you may need to consider investing into funds or other investments directly. ISAs are tax-privileged wrappers. Outside them there are potential tax charges, although for many investors they are not punitive. The two main taxes are:

Income tax – the first £5,000 of dividends in the current tax year are covered by a dividend allowance which is taxed at a nil rate. The excess is taxable at 7.5% for a basic rate taxpayer (or 32.5% and 38.1% respectively for higher and additional rate taxpayers). From 6 April 2018 it is proposed that the dividend allowance will fall to £2,000.

Investors may qualify for the Personal Savings Allowance of £1,000 (£500 for higher rate taxpayers) and possibly even the 0% starting rate of tax of up to £5,000.

Capital gains tax (CGT) – you have an annual CGT exempt amount of £11,300, which means that you only pay tax (at 10% for basic rate or 20% if a higher rate taxpayer) on gains in excess of that threshold. Gains on property are still taxed at 18% for basic rate and 28% for higher rate taxpayers.

Many investors use their annual ISA allowance by selling the investments they hold directly and reinvesting them into their ISAs, realising gains which may be fully or partially within the annual CGT exempt amount. So rebalancing your portfolio annually and keeping an eye on your ISA investment levels should help manage your investments efficiently.

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Funding a degree in debt?

The new academic year is about to start, with student debt firmly in the political spotlight.

"Students now graduate with average debts of £50,000."

So said the Institute for Fiscal Studies (IFS) in a recent paper examining higher education costs in England. The higher education financing rules differ for the other three constituent parts of the UK, but all rely upon undergraduate borrowing to some extent.

For a student in England starting a course this autumn, their level of debt on graduation is likely to be more than £50,000. In 2017/18, maximum tuition fees will increase to £9,250 a year, and the interest rate charged on loans will jump to 6.1%. The IFS calculates that on average students will accrue a £5,800 interest bill over the duration of their course.

Written off?

In England (and Wales) the loan currently starts to be repayable at the rate of 9% of income above £21,000, so a graduate earning £31,000 would pay £75 a month, which may not even cover the interest accruing on the debt. Fortunately, any outstanding debt is written off, but only after 30 years following the April in which the course ended. The IFS estimates that the government will eventually write off nearly a third of the interest and debt total, with fewer than one in four fully repaying their debt.

If you have children or grandchildren heading off to university at some point, these debt figures can appear daunting. Providing financial assistance by establishing a pre-funding arrangement often makes sense. However, careful consideration should be given to applying these funds directly to paying tuition fees and/or maintenance rather than initially drawing down the student loan.

In the worst scenario, upfront payment may simply reduce the government write-off. In other situations, there could be some logic in clearing the loan and avoiding high interest payments. Your funding plans therefore need flexibility built in.

Credit: Istock/martin-dm

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While other tax rules have tightened, the treatment of capital gains remains surprisingly generous, with a personal annual exemption of £11,300 of gains and a 20% maximum rate on virtually everything other than residential property. It's enough to give you second thoughts about investing for income…

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The financial challenge for ageing divorcees

The average age for divorce has reached an all-time high.

The average age on divorce is now nearly 46 for men and 43½ for women. This makes agreeing the financial settlement more challenging, because the higher the age, the more wealth there generally is to argue over. Some of that will often stem from rising property values, but another major (and sometimes forgotten) aspect is pension rights.

By their mid-40s, each party may have accumulated over 20 years the equivalent of hundreds of thousands of pounds worth of pension benefits, possibly including some from final salary schemes.

Dealing with pensions on divorce is a complex area that will inevitably require financial as well as legal advice. If you find yourself facing a divorce, do talk to us as soon as possible so that we can explain the tax and retirement ramifications that flow from the various pension settlement options.

The Financial Conduct Authority does not regulate tax or divorce advice. Occupational pension schemes are regulated by The Pensions Regulator.