WINTER 2015/16

first edition

Independent Financial Advice

NEWS AND ADVICE FROM BIRKETT LONG

Team leader, Nicola Ward, extends a warm welcome to this new newsletter:

Birkett Long has formed a separate subsidiary – Birkett Long IFA LLP – within the Birkett Long group. As far as existing clients are concerned, on a day to day basis you will see the same advisers and support team members. Birkett Long IFA LLP remains authorised under the Financial Conduct Authority (FCA) as Independent Financial Advisers. As many of you know our team celebrated its 25th Anniversary in 2014 and this move will allow us to further develop to ensure we continue at the forefront of financial services. This twice yearly newsletter will provide topical and informative news, which we hope you will enjoy. If there is any content you would like to see in future editions please let me know.

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High earners' pension relief cut

Following the 2015 summer Budget, those earning more than £150,000 will no longer qualify for an annual allowance of £40,000 (the annual allowance is the maximum that can be paid into a pension in a single tax year). Instead, high earners will see this allowance potentially reduced to £10,000. From 8 July 2015 those earning over £150,000 will see their annual allowance reduced by £1 for every £2 earned. On this basis, those earning in excess of £210,000 will have a reduced annual allowance of £10,000. This is a far cry from 2010/11 when the annual allowance was £255,000.

To compound matters, the change in legislation does not take into account the value of existing pensions. There will undoubtedly be some individuals who wish to put more into their pension, only to be prohibited by a much lower annual allowance.

So where does this leave high earners looking to plan for their retirement?

Additional rate taxpayers may need to consider other forms of saving towards retirement, making use of other tax breaks such as Individual Savings Accounts (ISA), Enterprise Investment Schemes (EIS) and Venture Capital Trusts (VCT), at the same time ensuring diversified arrangements are in place to suit their needs.

One option that could be considered is making use of 'carry forward', which enables individuals to look back at the last three tax years and bring forward any unused allowance in order to make additional pension contributions in the current tax year. The reduced annual allowance is likely to leave high earners with less ability to carry forward in future years, so it is important that those who are likely to remain high earners use this window of opportunity to their advantage. Carry forward, like an ISA allowance, works in a similar "use it or lose it" way, so if you wish to maximise your pension contributions, ensure you take action by the end of this tax year in order to take full advantage of this opportunity.

Contact us to discuss personalised solutions for pension funding options.

Pensions are a long term investment and the capital you invest can go down as well as up. You may get back less than originally invested. Pensions tax legislation can and may change in the future.

Lower risk investment opportunities

With the Bank of England base interest rate held at a record low level of 0.50% for over six years, investors with bank and building society cash Individual Savings Accounts (ISAs), despite the tax free status, have been particularly affected.

Many people who have held variable rate cash ISAs for a number of years typically can be receiving an interest rate of between just 0.1% and 0.5% per annum. Often a very attractive introductory bonus rate has been provided for the first six to twelve months, but then the rate is dropped substantially.

It is often possible to transfer an ISA without charge. However, alternative bank and building society cash ISA rates, whether variable or fixed, will generally still result in value being lost in real terms, once inflation has been taken into account. Fortunately there are other alternatives available.

Deposit based structured products have become popular as an attractive, lower risk investment option. Deposit plans offer the opportunity of an investment protected by the Government's Financial Services Compensation Scheme (FSCS), up to £85,000 per individual, reducing to £75,000 from January 2016. These plans can be held either as an ordinary investment (with returns being subject to income tax liability), or as an Individual Savings Account. It is also possible to effect ISA transfers to these plans. Returns on deposit plans are potentially more attractive and could produce, for example, 4% to 4.5% per annum.

Structured deposit plans aim to pay out the full maturity value subject to certain conditions being met. This may be a (Stockmarket) index being a certain percentage amount higher at maturity compared to the Initial Index starting level of the plan. However, in many cases should the index be lower at maturity, only the original investment would be repaid, albeit in full. A number of deposit plans now have a kick-out facility, which typically provides several points at which the plan can mature/pay out subject to the particular index level being higher than at the outset.

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Finances on divorce

The legal position

When a couple enter into a marriage they are undertaking a duty to support one another, both emotionally and financially. What many spouses do not know is that, in the event of separation, whilst the emotional duty may come to an end, the duty to financially support their spouse and family does not.

Whether a separating married couple decide to divorce or not, the duty continues until such time as the court formally dismisses it.

This can result in one spouse having to provide the other with monthly payments, known as spousal maintenance, and possibly child maintenance. If one spouse has a higher income than the other a great deal of conflict can arise as to what amount, if any, should be paid each month.

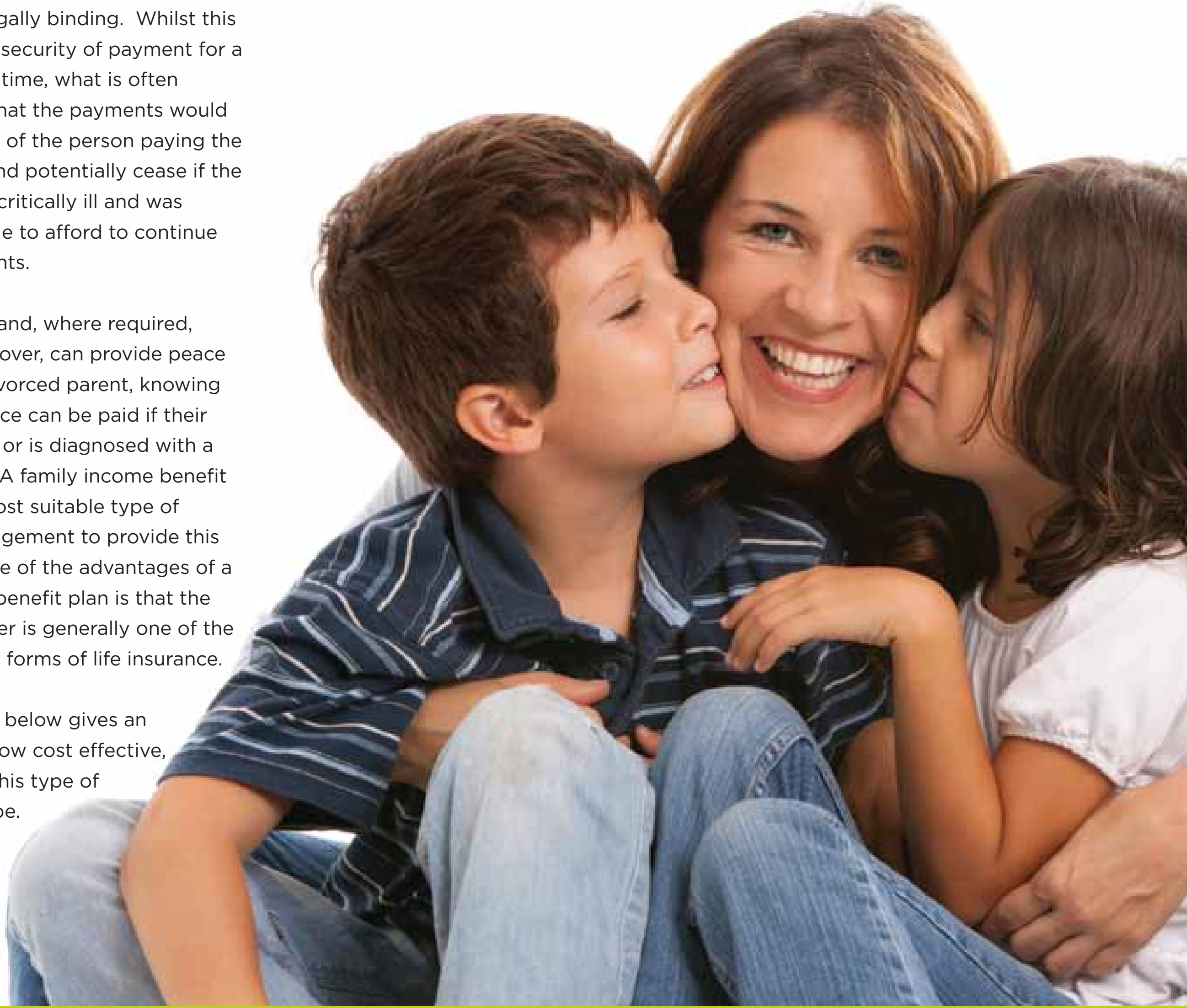
If you believe you may be entitled to spousal maintenance and/or child maintenance or think you may have to pay it, you should try and seek advice at an early stage; this can minimise any dispute and ensure everyone knows where they stand at the outset.

Child maintenance

Maintenance payments often form part of a divorce settlement and can therefore be legally binding. Whilst this provides some security of payment for a fixed period of time, what is often overlooked is that the payments would cease on death of the person paying the maintenance and potentially cease if the payer became critically ill and was therefore unable to afford to continue making payments.

Life assurance and, where required, critical illness cover, can provide peace of mind to a divorced parent, knowing that maintenance can be paid if their ex-spouse dies or is diagnosed with a critical illness. A family income benefit policy is the most suitable type of insurance arrangement to provide this protection. One of the advantages of a family income benefit plan is that the cost of the cover is generally one of the least expensive forms of life insurance.

The case study below gives an illustration of how cost effective, and essential, this type of insurance can be. To find out more, give our team a call on 01206 217309.



Case study

Family Income Benefit insurance

Sue and Graham Smith have divorced. They have a daughter, Millie, aged six and a son, Thomas, aged nine. The couple have agreed that Millie and Thomas will live with Sue, and Graham will pay £900 maintenance per month (£450 for each child) until they are 18.

Sue could protect those maintenance payments with life and/or critical illness cover under a family income benefit policy on the life of Graham. If Graham died prematurely or became critically ill and was unable to make the maintenance payments, the children would continue to be cared for financially.

In this example, just £36.16 each month will give Mrs Smith peace of mind. This would consist of two separate arrangements, one to provide for Millie, and one for Thomas. Once Thomas reaches age 18, the maintenance payments will stop, but the cover for Millie's maintenance payments will continue until she reaches age 18. Therefore after 9 years, when Thomas reaches age 18, the cost of the cover will reduce to £20.47 each month, as the premium to the policy for Thomas will stop.

It is also possible to protect the maintenance payments from inflation by incorporating indexation into the arrangements.

This inexpensive type of cover can provide peace of mind that your children will not be financially disadvantaged. Can you afford to ignore it?

under the spotlight

Pensions are not like bank accounts after all!

Following the implementation of the pension freedom rules in April 2015, tabloid headlines have given us the impression that pensions now operate like a bank account. Although pensions have become more flexible, the reality is that they cannot be treated as bank accounts.

Potential problems when considering withdrawing funds from a pension plan include taxation implications and reducing your ability to pay more into a pension.

When a pension withdrawal is made, in addition to the 25% tax-free cash entitlement, HMRC assumes that similar sums are going to be withdrawn regularly in the future. For example, after payment of tax-free cash, a one-off £10,000 payment will effectively be treated by HMRC as though £120,000 is due to be taken (i.e. £10,000 x 12 months). In most cases, too much tax will be deducted from the payment, resulting in a less than expected net withdrawal initially. In order to obtain a refund, a form will need to be completed and sent to HMRC.

As covered earlier in this newsletter, the maximum amount that can be paid into a pension per tax year is £40,000. There are often justifiable reasons for someone over the age of 55 to access their pension early, even whilst still working, but future ability to contribute to a pension should be considered if the amount being withdrawn is in addition to the tax-free cash entitlement as a lower annual allowance of £10,000 then applies. Whilst that may offer sufficient scope for most people, having that sum reduced to £10,000 may leave some individuals with an unexpected tax bill.

In light of the pension freedom rules, another area for consideration is what happens to the pension pot on death. Bank accounts form part of an individual's estate, and such assets are passed to beneficiaries in accordance with their will.

Pensions operate differently, however. If there is no surviving dependent when a pension policyholder dies, the beneficiary will be at the pension provider's discretion. Although these rules provide new planning opportunities when passing on a pension legacy, individuals should give thought to the beneficiaries and to the tax implications for individuals who die after the age of 75. Existing pension arrangements should either be written under trust or have an up to date Expression of Wish or Death Benefit Nomination in existence to ensure that benefits are payable in accordance with the policyholder's wishes.

At Birkett Long IFA, we work closely with our colleagues in the wills, trust and probate team to ensure our clients receive 'joined-up' advice.

The financial conduct authority does not regulate wills and estate planning.

ISAs - don't forget

- ISA allowances work on a "use it or lose it" basis, so don't forget!
- The maximum ISA contribution for the 2015/16 tax year is £15,240.
- Money can be held in cash and/or stocks and shares investments.
- Contributions for the 2015/2016 tax year can be made up to 5 April 2016.
- Remember that ISA arrangements can be transferred to other providers to obtain potentially better returns.

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