FinancialLandscape

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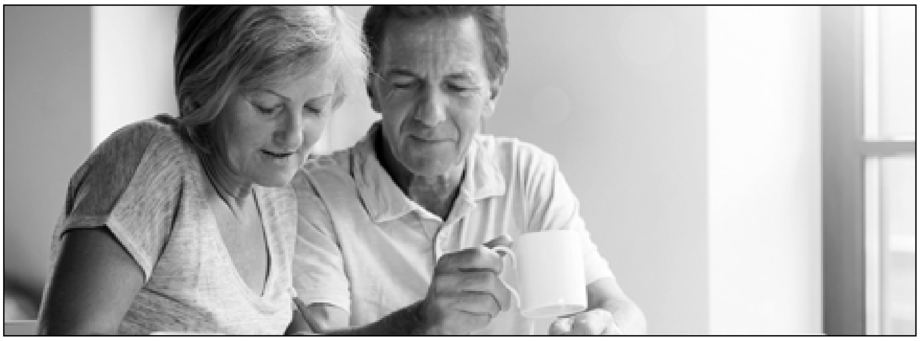
Pension reforms

How the lifetime allowance reduction could impact on your retirement savings



The Government has introduced comprehensive reforms to the pension rules over the previous few years. One important change, which may have been overlooked by some savers, is the reduction of the lifetime allowance that applies to pension savings. The lifetime allowance is the total amount you can hold within all your pensions without incurring an additional tax charge.

INFLATIONARY INCREASES

The Government has indicated that this allowance will increase each year in line with inflation (CPI) but only from 6 April 2018. It was reduced from £1.25m down to £1m from 6 April 2016. If you have more than £1m in your pension pot or are likely to do so at retirement, you can apply to protect it against reductions to the lifetime allowance.

TAKING ACTION

While some people may not be affected by the lifetime allowance, it's important to take action if the value of your pension benefits are approaching, or are above, the lifetime allowance. As pensions are a long-term commitment, what might appear modest today could exceed the lifetime allowance by the time you want to take your benefits.

TAX CONSEQUENCES

Exceeding the lifetime allowance could have significant tax consequences, for example, any lump sum withdrawals you take from the excess amount within your pension are taxed at 55%, and if you retain the excess amount within your pension fund a 25% tax charge is made (and any income taken from the fund will be taxed at your marginal rate of Income Tax).

FIXED PROTECTION

If you could be affected by the reduction in the lifetime allowance, there are some actions you could take to help protect yourself from this potential tax charge. However, if you have accrued pension benefits since 6 April 2016, fixed protection will not be available, so you should obtain professional financial advice to look at the options available to you.

TAKING BENEFITS

If you are already taking benefits from a pension, this will also impact your lifetime allowance. It is important to note that the allowance applies to the value of your pension when you eventually come to draw money from it (and not the value on 6 April 2016). This means that even if your pensions are currently worth well short of the new £1m limit, you could still be affected by the reduction and may need to take action now, even if you think the reduction does not currently really affect you.

HIGH EARNERS

Another pension change which came into effect from 6 April 2016 is a reduction to the annual allowance for high earners. The allowance of £40,000 will reduce by £1 for every £2 of income received above £150,000 (the threshold for the additional rate of Income Tax). The reduction is limited to £30,000, meaning anyone with income of £210,000 or more will have a £10,000 annual contribution allowance. Bear in mind that 'income' for this purpose includes employer pension contributions. ■

ARE YOU ON TRACK TO BREACHING THE ALLOWANCE?

While £1m may sound like a generous sum, it is surprisingly easy to breach this limit, meaning that you could be subjected to a tax bill of up to 55% on some of your pension pot. Whether you're a saver in the middle of your working life or nearing retirement, it's crucial you know if you're on track to breaching the allowance. If you have any concerns and would like to discuss your situation, please contact us.

A PENSION IS A LONG-TERM INVESTMENT. THE FUND VALUE MAY FLUCTUATE AND CAN GO DOWN, WHICH WOULD HAVE AN IMPACT ON THE LEVEL OF PENSION BENEFITS AVAILABLE.

YOUR PENSION INCOME COULD ALSO BE AFFECTED BY INTEREST RATES AT THE TIME YOU TAKE YOUR BENEFITS. THE TAX IMPLICATIONS OF PENSION WITHDRAWALS WILL BE BASED ON YOUR INDIVIDUAL CIRCUMSTANCES, TAX LEGISLATION AND REGULATION, WHICH ARE SUBJECT TO CHANGE IN THE FUTURE.

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Financial planning for people and business.

Investment matters post-Brexit

Facing new challenges at every turn to meet long-term objectives

We are now living in a more uncertain world, and for many investors they are facing new challenges at every turn. As correlations between asset classes rise, the right strategy is crucial to preserve capital when markets are falling. Add to this the result of the European Union (EU) referendum, which came as a shock to financial markets, there is likely to be fallout from this historic event for some time. So what can you do to manage your investments in current markets?

MARKET CONDITIONS

With heightened volatility looking like it could be with us for some time, much will depend on what happens politically and how central banks respond over the coming months. Political uncertainty is likely to continue for some time, particularly in the UK, but also in Europe and elsewhere further afield. This could affect economies globally, with the UK potentially going into recession by next year.

BETTER EQUIPPED

On a more positive note, the banking sectors globally are more stable than they were back in 2008, with governments and central bank policies being more supportive. Bank capital levels are substantially higher than they were in 2007/08, and UK and European banks are much better equipped to weather volatility.

INVESTMENT STRATEGY

It's important not to react out of panic and where possible to remain calm and take a long-term view. Taking a step back from the short-term noise, thinking about why you invested in the first place and making sure those reasons haven't changed are essential before making any decisions about implemented changes to your current investment strategy.

ROUNDED APPROACH

Successful investment requires the navigation of complex market forces, economic, political and behavioral factors (as well as company financials). So it's important to take a more rounded approach. The single most important thing you can do to mitigate risk is to diversify your portfolio. You may already invest in different types of investments across different countries, and if that is the case you should be well diversified and with someone making the day-to-day investment decisions for you.

INVESTMENT REASONS

If you actively manage your own investments, you'll probably want to make sure your choices still meet your needs and your original reasons for investing are still valid. You should also consider taking professional financial advice. Some of the questions you might want to ask are: are you suitably diversified to help shelter your money from significant volatility? If you're invested in a riskier single asset class or region, did you deliberately take this approach? Is it still right for you in the current market environment?

3 TIPS TO MAXIMISE YOUR INVESTMENT RETURNS

1. Consider investing in a wider range of asset classes
2. Be more adventurous with your strategic position
3. Take a more flexible approach to different opportunities

RETIREMENT MATTERS

If you're still some years from retirement, your pension investments will have time to recover from any short-term losses. Even if you're near retirement or are already retired and relying on your investments for income, you shouldn't panic. There are things you could do to help shelter yourself from market volatility.

If you're approaching retirement, the most important thing to do is make sure you're in investments that will get your money to where it needs to be by the time you retire – whether that's purchasing an annuity, taking it all out as a lump sum, or keeping it invested and taking a flexible income.

If you're already retired, there are also ways to help protect your money not just from market volatility but throughout your retirement. ■

HELPING YOU TO MEET YOUR LONG-TERM COMMITMENTS

With persistently low inflation, ultra-low interest rates, low growth and low returns, some investors may not be feeling the reward potential that heightened risk brings. In a low-yield environment, how can you meet your long-term objectives? To discuss the options available to you, please contact us to discuss your requirements.

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Savvy investors

Time to get wrapped up? How to shelter income and capital gains

For long-term investors, Individual Savings Accounts (ISAs) are a very tax-efficient wrapper that can hold cash savings as well as investments in stocks and shares. Savvy investors are also able to shelter income and capital gains.

ISA FLEXIBILITY

The limit on how much can be saved in an ISA each year has doubled since 2009; you can add up to £15,240 to an ISA in the 2016/17 tax year. Cash that you withdraw from a flexible ISA can be replaced during the same tax year without counting towards your annual ISA allowance, which is known as 'ISA flexibility'. What sets ISAs apart from other savings and investment accounts is that any interest on cash savings, gains from investments or income from dividends are tax-efficient, and you don't have to declare ISAs on your tax return.

ADDED ADVANTAGE

Because of their tax benefits, ISAs can help your savings and investments grow faster over time. Investing your ISA in stocks and shares has the added advantage of helping safeguard you from a potential Capital Gains Tax (CGT) bill in the future. CGT is a tax on the gain you make when you sell or dispose of assets such as investments. It is currently charged at 20% for higher-rate taxpayers on gains made that exceed the yearly tax-free allowance. Currently, the CGT allowance is £11,100.

ADDITIONAL ALLOWANCE

Rules on ISA death benefits introduced in April 2015 allow for the transfer of an extra ISA allowance to the deceased's spouse if they passed away on or after 3 December 2014. The surviving spouse can use an additional one-off allowance, which is equal to the value of their partner's ISA savings, as well as enjoying their own usual yearly allowance. An additional permitted subscription (APS) can be used for up to three years from death.

INHERITANCE TAX

You qualify for the additional allowance whether or not you inherit the actual assets of the ISA. The deceased's ISA assets are distributed according to the terms of the will or intestacy rules, and any Inheritance Tax liability will remain in the usual way (except ISAs qualifying for Business Property Relief, for example, Alternative Investment Market [AIM] ISAs). No actual funds are transferred, and the extra allowance can be made up from your own assets. Also, as well as being married or in a registered civil partnership with the ISA holder, you need to have been living together – if you were separated, either under a court order, Deed of Separation or any other situation that was likely to become permanent, you can't use the additional allowance.

COMPOUNDING EFFECT

Long-term investors that can afford to invest at the start of the tax year rather than at the last minute not only gain a year's performance, but these extra gains will be reinvested in the market until they need the money. Over time, the effect of compounding can be significant. The more you invest, the greater the potential impact of early investing. Likewise, the longer you are investing for, the larger the compounding effect. Also, investing early in the tax year to benefit from compounding is most pertinent not only for those saving for retirement but also for parents investing for their children's future through dedicated Junior ISAs (JISA). ■

BUILDING A LONG-TERM INVESTMENT STRATEGY

If you are unsure about the suitability of your investments, you should always obtain professional financial advice. For the effects of compounding to work requires two things: the re-investment of earnings, and time. The more time you give your investments, the more you are able to accelerate the income potential of your original investment, which takes the pressure off of you. To discover how we can help you build a long-term strategy for your investments, please contact us – we look forward to hearing from you.

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Empty nest, empty wallet

Parents putting financial health at risk to fund university costs

When it comes to funding a university education, it is parents and grandparents that typically look to provide the money. But even though this may be the case, last year's graduates from English universities still left with an average of £44,000 debt (source: Sutton Trust), with some parents still, on average, expecting their children to leave university with £23,000 debt.

Students are closer to the mark, predicting an average debt of £35,000. Students expect, on average, to take 17 years to pay off their debt once graduated; research from the Sutton Trust suggests three in four graduates will be paying off student debts into their 50s.

EMPTY NEST, EMPTY WALLET

While a substantial number of parents (61%) seem willing to help with the financial costs of university, rising to 73% for Londoners and a low of 47% in the South West, a significant proportion (78%) of these will be relying on their own cash savings.

Some 62% of parents say they will use a proportion of their cash savings, while 20% will be putting themselves potentially at financial risk, saying they or their child's other parent will use all or most of their cash savings. 9% of parents said they or their child's other parent would take out a bank loan in their own name to help fund their child's university costs – something that seems particularly drastic – and 8% of parents said they would sell shares or other financial investments.

PARENTS OVERESTIMATE AMOUNT NEEDED FOR REGULAR SAVING IN STOCK MARKET

Most parents look to cash savings to fund their children's university costs, and there is a perception that quite large sums of money are required to invest in the stock market. Parents estimated, on average, that the minimum amount required to invest monthly in an investment saving scheme was £81.51 per month, when in fact the minimum amount required to invest in a children's investment company savings scheme is much less, namely £25. Parents in the 35–44 age bracket overestimated this figure the most (£91.76 per month), and of course it's this group who are likely to have the most time on their side.

The research suggests that many parents massively underestimate the amount of student debt their children will graduate with. Parents are willing to make huge financial sacrifices to help their children through university, and many grandparents are sharing the financial burden.

BANK OF GRANDMA AND GRANDPA

A fifth (20%) of grandparents are contributing or planning to contribute to children's university costs, to the tune of £2,402 on average per year. A quarter (25%) of grandparents are already contributing financially to everyday family expenses, and of these 12% of parents say that their child's grandparents currently contribute financially to holidays, 4% to school fees, and 3% respectively to building projects and childcare, while 2% are contributing to a property deposit.

AN EDUCATION OR A FIRST HOME?

Interestingly, one third of students (33%) said that they had a savings and investment scheme which their families had 'earmarked' for their future. Half of these (51%) wanted the money to go towards their first property, 44% wanted to spend it on university costs and a free spirited 16% wanted to spend the money on travelling. ■

Source data:
The research was conducted by Opinium from 8–16 June 2016 amongst 1,006 UK parents with children aged 13–18 that are planning to go to, or are already at, university, and 1,014 UK full-time students planning on going or currently at university.

WANT TO ASSESS THE OPTIONS AVAILABLE TO YOU?

Current university students may face leaving with massive debts as well as a degree, but parents can act now to ease the financial burden. It's crucial not to be afraid to seek professional advice. We can assist you to get a clearer idea of the opportunities and drawbacks involved in making further education-related choices. If you would like to assess the options available to you, please contact us for further information.

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