HDA
Chartered Financial Planners

News and Views

Spring 2017

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Welcome to our Spring newsletter. A few articles to educate, amuse, provoke? It's a great time of year as the evenings get lighter and the flowers bloom. It's also the time to run through your financial checklist:

ISAs – this year's allowance is £15,240. Use it by 5th April or lose it forever. Tax-free income and growth. Nothing to report to the tax man. Don't miss out.

Pensions – unbeatable value: tax relief at your highest rate, tax-free growth, tax-free lump sum from 55 onwards. Even tax relief for non-tax payers! A massive benefit that is coming under ever greater threat from the Government. You can carry forward allowances for three years only so your 2013/14 allowance will be lost forever from 5th April unless you use it.

Capital Gains – are your investments growing? If they are not in pensions or ISAs you may be accumulating taxable gains. Be sure to use this year's Capital Gains Tax exemption (£11,100 for individuals, £5,550 for Trusts) before 5th April.

Gifts – are you trying to reduce future Inheritance Tax liabilities? You can give away £3,000 every year and the gift will be immediately exempt. You can go back one year if you didn't take advantage last year.

Risk – Are your investments in the right place? In 2016 we witnessed some unexpected events and these have influenced markets and currencies globally. Remember that HDA offers an almost unique risk-management process. You will never have more risk in your portfolio than you have told us you want and the returns you achieve (up and down) will reflect that.

Review – As we move into the new financial year what better time to review your future planning. What are your goals? Are you on track? Are you doing the right things? Speak to your adviser today.

As ever, we welcome your comments and feedback. We look forward to speaking to you soon.

Are you alright there?

I know a lot of financial advisers. It's a terrible thing to say but I wouldn't trust most of them with my kids' pocket money. I don't like the suits they wear. I don't feel like I'm part of their club – you know, the one where they talk a lot about football and the last curry night they had and those super-wealthy jet-set clients they hobnob with. I get the same uncomfortable feelings when I go into a car dealership or an estate agent. Or when I go into a shop or bar and that disinterested voice says "Are you alright there?". What does that mean, anyway? Whatever happened to "May I help?" or "What can I get you?".

So, if I don't like or trust most financial advisers – then what hope is there for the general public? When I say that I don't trust them, I don't mean that they would run off with your money. I mean that I'm not at all convinced that they put your interests before their own. To them, clients are a commodity. The service they provide is commoditised. They, themselves, are commoditised by the companies they work for. Legions of self-employed drones working to a template for the greater good – but who's greater good?

Here's the thing. I also know some really good financial advisers. They are mostly unassuming. Usually very hard working. They are not the type of people who would sell you houses or cars. No offence to those who do – your job is to sell product and to be paid for the sale. Don't pretend to be our best friend or to be imparting worldly wisdom – you're just trying to make a sale. Which is fine.

The good financial advisers are also good salesmen. But what they are selling is advice and it is not a one-time deal. They have to give a life-long warranty and be prepared to back it up with excellent service. They can't pretend to care – they really have to care. They have to be prepared to go on the journey with you and to share your hopes, fears, uncertainties and ambitions. It's not a job. It's a vocation.

Experience and qualifications count for a lot but, to find the good advisers, you have to be able to get past the noise.

I can't tell you exactly how you do that. But you've got our phone number. The same one we've had for the past thirty years. Or you could ask some of the clients that have been with us for most of that time. The ones whose lives we have already changed, whose journey we are still sharing.

Had we but time enough

When pensions freedoms were introduced in April 2015 the number of annuities being purchased fell dramatically. Flexibility and control were seen as by far the more attractive option, especially as annuity rates had dropped to such low levels.

Annuity rates are linked to long term Gilt yields. Over the past decade rates have fallen from over 5% to below 1% in the Spring of 2016. Rates have been driven to such low levels by an economic policy of low interest rates and Quantitative Easing. Whilst rates have "rallied" to c. 1.7% at the present time they are likely to remain close to their all-time lows for some time to come.

For a healthy 65 year old couple, £100,000 will currently buy a guaranteed level annual income of c. £5,000. That means it will take 20 years just to get their money back (ignoring tax!). That doesn't seem a good deal – particularly as there is no access to capital and no way to change the terms of the annuity once it has been purchased.

What the annuity does provide, however, is an insurance policy against living longer than average. The income is risk-free and will continue to be paid even if the annuitant lives well beyond his or her telegram from the Queen. For there to be an average life expectancy of 85, some people must live well beyond that age. Be mindful of the 'flaw of averages'.

Inflation-proofed annuities may also have a part to play in some people's future planning. Starting rates of income are desperately low at just under £2,500 per £100,000 but future economic change could see this additional "insurance" element pay dividends. Who is to say that the high inflation rates of the 1980's will never make a comeback?

In the short term, locking your money up in a low-yielding, fixed-income product such as an annuity is unlikely to make sense. But stay alert. Markets, interest rates and inflation will all change over time. The price of pension freedoms may be very low at present but that may not always be the case.

Should I stay or should I go now?

For many years, Independent Financial Advisers have considered transferring benefits out of a Final Salary (Defined Benefits) Scheme to be a very bad idea. However deferred scheme members have seen transfer values (known as Cash Equivalent Transfer Values or CETV's) rocket because of BREXIT, the fall in the value of sterling and the resulting fall in Gilt yields. This increase has meant that the decision on whether to transfer out of a Final Salary Scheme has become much more finely balanced.

In the past, there was often little logic in transferring away from a Final Salary Scheme because of the requirement for the transferred funds to be used to buy an Annuity (a similar guaranteed income) from age 75. Taking 'ownership' of the transferred funds was therefore short-lived. The introduction of the Government's Pensions Freedoms legislation on 6th April 2015 has changed the landscape completely. While the new legislation had no impact on Final Salary benefits, complete flexibility is now available with Personal Pension funds.

The Financial Conduct Authority (FCA) has not laid down any specific new rules in the light of the change in legislation, but does accept that there are several reasons why clients may now wish to consider transferring out of a Final Salary Scheme. Some of the reasons are:

- Transferred funds become an asset of the individual. Final Salary Schemes provide a lifetime income (known as a Scheme Pension) from the scheme's assets. The scheme member never actually owns the asset.
- Following a transfer, the member can take 'what they want when they want' from their fund. Final Salary benefits are index-linked in payment and cannot be altered.
- The amount of tax-free cash available from a transfer is often higher than the amount available from a scheme. Outstanding debt repayment such as paying off a mortgage can influence the amount of tax-free cash required at retirement.
- Death benefits are often significantly higher if benefits are transferred. This is particularly true if the member is single at the time of death.
- Following a transfer, benefits can be left to a dependent or anyone else that the policyholder wishes to nominate. Final Salary benefits can only normally provide benefits to a dependent (i.e. a spouse or dependent children of the member)

Future investment returns are the main risk associated with transferring away from a Final Salary Scheme. Poor returns and high withdrawals may mean that funds run out before death. Final Salary Schemes provide peace of mind because the income is index-linked and guaranteed.

Where transfer values from Final Salary Schemes exceed £30,000, it is now a legal requirement for advice to be sought. There are many aspects to consider and at HDA we are very experienced in explaining all the pros and cons.

If you are interested in reviewing your pension situation, please contact us.

Note: This article only relates to Deferred Final Salary Scheme benefits. If you are an active Final Salary scheme member you should always remain in the scheme.

I don't believe it…

I am starting to sympathise with Victor Meldrew. Since I turned 50 more and more things seem to drive me mad. I spoke to a client the other day who told me that pensions were a waste of time and the only sensible investment was residential property. So I ran through some figures:

- £80,000 profit from his business suffers Corporation Tax of £16,000 which leaves £64,000
- He is already a higher rate tax payer so a £64,000 dividend will suffer tax of £20,800 which leaves £43,200 to invest in property.
- Or he could put £80,000 straight into his pension (using carried forward allowances).
- At retirement, he can withdraw £20,000 tax-free. Assuming he is then a basic rate tax payer the balance will suffer tax at 20%. That leaves £68,000 net in his pocket.
- That is 57% MORE than the dividend route.

So he took my advice and made the pension contribution. I saved him £24,800.

Then he asked me to waive my £800 fee. ...I don't believe it!

Sigh of Relief

In recent years, pension allowances and reliefs have gradually been squeezed. Further cutbacks are on the horizon and so, as the end of the tax year draws near, now is the time to take maximum advantage.

Pensions are still the most tax-efficient way to save for retirement - it doesn't matter if you are self-employed, employed, a business owner or even retired. Eligible contributions to an approved pension plan are subject to tax relief at your marginal rate:

- 20% for Basic Rate Tax Payers
- 40% for Higher Rate Tax Payers
- 45% for Additional Rate Tax Payers
- 60% if earned income is between £100,000 and £122,000

There are now just a few weeks to take advantage of some of the pension saving incentives which will be lost in April 2017:

Annual Allowance (AA) Carry Forward
Carry forward allows you to make use of the balance of unused allowances from the three previous tax years (earliest first). In 2013/14 the Allowance was £50,000. That will be lost on 6th April if not used in full.

Money Purchase Annual Allowance (MPAA)
If you have cashed in a pension plan or flexibly accessed income from pension funds, you cannot carry forward any previous year's Annual Allowance. Instead, the MPAA limit applies which is currently just £10,000. From the 6th April 2017, it gets worse - the MPAA will reduce to just £4,000 per annum.

Tapered Annual Allowance
If your income from all sources (including employer pension contributions) is over £150,000, your £40,000 Annual Allowance will be reduced by £1 for each £2 above the threshold. The minimum Allowance will be £10,000 (when income reaches £210,000).

However, if your income excluding employer pension contributions and net of any personal pension contributions is below £110,000, the taper will not apply. A large personal pension contribution using carry forward could bring your "threshold income" below £110,000 and restore your full £40,000 Annual Allowance for 2016/17.

Employer Pension Contributions
With Corporation tax rates due to fall from 20% to 19% on the 1st April and further cuts expected over the next 3 years, now is the time for business owners to maximise pension contributions to benefit from higher rates of tax relief.

If you would like to talk to an Adviser then contact us using the telephone number below or online using our Contact Us page

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