

moneyworks

The essential consumer guide to making your money work harder.

Winter Edition

Are you ready for the challenge?

A look at what to expect in 2016 and how to make your money work harder.

Time to take control

Are you getting the most out of the pension reforms and is now the time for a change?

Legacy for loved ones

Why you can now leave your pension to loved ones in a tax-efficient way.

Second-hand annuities

How you could escape from a poor value annuity.

Welcome

Happy New Year and welcome to the latest issue of **moneyworks**, the quarterly consumer publication which brings you the current financial issues and stories in the news.

Following a tough year for investors in 2015, there is speculation that this year could be just as challenging. With this in mind we take a look at the major reasons for uncertainty over the coming 12 months and how you might remain in a strong financial position with the right planning and advice.

Following the pension reforms we look at how the new rules have made leaving your pension as an inheritance to your loved ones a much more favourable financial option, and why if you have just a few more years left in work, now is the time to take control of your pension options.

We also look at new Government plans to help people who are trapped with a poor value annuity and how to get a better deal by shopping around for a second hand one.

Here's wishing you a happy, healthy and very prosperous 2016.

Best wishes

The **moneyworks** team

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The News in Brief

A round up of the current financial stories.

Property prices set to soar by 2025

House prices enjoyed another strong year in 2015 – and a new forecast suggests that they will rise by another 50% over the next decade.

In December 2015, the National Association of Estate Agents and the Association Residential Letting Agents revealed that they expect average UK house prices to increase from £280,000 to £419,000 by 2025. London properties are predicted to nearly double to £931,000.

Meanwhile the Office of National Statistics has reported that the average house price across the UK was £287,000 in October – a 7% rise on a year earlier. In England, the cost of a typical home reached £300,000 for the first time.

(Sources: <http://www.bbc.co.uk/news/business-35102130> and <http://www.ons.gov.uk/ons/rel/hpi/house-price-index/october-2015/statistical-bulletin.html>)

Only one in 10 self-employed people are saving for retirement

If you are self-employed, there are all manner of priorities to juggle in operating your business – but, worryingly, 90% are neglecting their own personal future.

According to figures from the Office for National Statistics, disclosed in December 2015, just one in 10 self-employed people are saving into a pension. This compares to a third who were in 2001. Further research from the Money Advice Service found that 53% of self-employed men, and 67% of self-employed women, have no pension savings at all.

Understandably – with your own business consuming so much of your focus – the future might be something that you haven't adequately considered. Without an employer helping you to set up and contribute into a pension, you may be lacking provisions to fund retirement. But this could mean you face major problems when you come to want to retire.

(Sources: <http://www.dailymail.co.uk/money/pensions/article-3342361/Just-one-ten-self-employed-workers-save-pension-compared-2001.html> and <https://www.moneyadviceservice.org.uk/en/articles/pensions-for-the-self-employed>)

The Bank of Mum and Dad

True financial independence does not begin until your mid-30s, according to December 2015 research by Skipton Building Society.

The poll of 2,000 UK adults, aged over 35, found that 25% admitted they did not feel financially stable by the time they turned 35, and still relied on help from their parents. 70% said they felt indebted to their parents for this support.

However, from their late 20s/early 30s, many attempt to readdress the balance. Six in 10 try to pay for family treats such as restaurant meals, 25% contributed to their parent's rent and 15% helped with their debts. A third of respondents also said they had refurnished or redecorated their parents' home, and another third treated them to new clothes.

Over half of those surveyed now cover the costs of special family events, such as birthdays and Christmas.

(Sources: http://www.ons.gov.uk/ons/dcp171778_415334.pdf and <https://uk.finance.yahoo.com/echarts?s=%5EFTSE#symbol=%5EFTSE;range=5y>)

It's good to talk

One in five British couples, over the age of 40, are potentially storing up problems when they retire by failing to discuss their financial plans with each other.

According to Prudential, who undertook this survey in October 2015, 49% of couples have no idea over the level of retirement income they can expect to receive when they stop working, and 27% don't know how much money their partner has in pension savings.

Just two in five couples have made arrangements for one partner to continue to receive an income in retirement, should the other die – 12% have never discussed leaving an income in retirement for each other.

(Source: <http://www.yourmoney.com/retirement/couples-risk-retirement-by-avoiding-financial-planning>)

Shades of grey

It's one sign of growing old that everybody dreads – and a new survey suggests it springs one in five of us into action. According to December 2015 research by AdviserWill.org.uk, a fifth of British people, aged 18-40, don't think they will consider arranging a Will until they sport their first grey hairs. Until that point, many don't see the need of having one, even though they are likely to have already passed key milestones, such as getting married, buying a house, or having kids. On average, the majority (57%) of respondents who had made a Will did so at the age of 38

(Source: <http://www.mirror.co.uk/news/uk-news/brits-urged-put-affairs-order-6989804>)

How to weather the storm

2015 was undoubtedly a difficult year for investors. Significant global events sparked market falls that few regions were immune from, and there are fears of more of the same in 2016. Here we look at five key areas, which could benefit or have a negative effect on how your finances perform this year.

Take advantage of available tax benefits

If you have not utilised your 2015/16 ISA allowance yet, you are running out of time. Fail to use the full £15,240 allowance by Tuesday 5 April, and it will no longer be available for storing your savings and investments in a tax-efficient wrapper. Inside an ISA, you don't pay tax on the returns your money generates, with the exception of a 10% dividend tax on stocks and shares ISAs, which is already deducted.

From 6 April, a new ISA allowance (also £15,240) will be available, and you and any partners may wish to utilise these allowances too. If you have a partner, make sure they use theirs also – so you can make even more tax savings.

Pension tax relief changes – real and speculated

From April this year, the amount that additional rate taxpayers can save into a pension sees changes. Individuals are able to receive tax relief on contributions up to their 'relevant UK earnings', subject to having sufficient available annual allowance (which would include any available to carry forward).

Some taxpayers could see their annual allowance reduced to £10,000 in circumstances where income reaches £210,000.

Higher rate taxpayers might also experience some bad news in 2016, with the Government due to report back on a consultation over tax relief.

At the moment, higher rate taxpayers benefit from 40% tax relief, but it has been suggested that a new flat rate of 30% will be introduced for basic and higher rate tax payers.

Good news for basic rate taxpayers, who currently only receive 20% tax relief, but it would become less rewarding for higher rate taxpayers to save into a pension.

Financial unrest in China

After decades of unprecedented growth, in recent years China rose to the position of the world's largest economy – which means the economic issues it has recently endured have had a ripple effect across the globe. Severe financial volatility at the beginning of the year brought the country's stock market to its knees and all eyes will be looking at China over the coming months.

Brexit

Following last year's General Election, Prime Minister David Cameron pledged to hold a referendum over Britain's continuing membership in the European Union (EU) by the end of 2017. There is a lot of speculation that the vote will be held this year.

As the referendum approaches, the possibility of market volatility will increase. Britain leaving the EU – dubbed 'Brexit' – would mark a huge change in relations with Europe; although a vote to stay in the EU could result in nothing changing.

Interest rate movements

With the US finally electing to increase interest rates at the end of 2015, the question is when the UK will follow suit. The Bank of England Governor, Mark Carney, has consistently been open and honest on this matter, in a bid to ease any market jitters about a sudden hike.

When a UK rate rise finally occurs, it will be a test of the economy's powers of self-sustaining recovery.

[Sources]

<http://uk.businessinsider.com/oil-price-falls-to-11-year-low-january-6th-2016-1>

The value of investments can fall as well as rise. You may not get back the full amount originally invested.

The tax treatment depends on the individual circumstances of the investor and may be subject to change in the future.

Legacy for loved ones

The recent changes around pensions mean they have become more attractive for your loved ones to inherit – which could prompt you to re-think how you approach your future.

Building up a large pot of pension savings could lead to a more fulfilling retirement – and it can now also provide a lasting legacy for your family. As part of the sweeping pension freedom reforms that were introduced in April of last year, the rules around inheriting a pension have been changed significantly, and it is something you might want your loved ones to benefit from.

Under the old rules, the tax charges around inheriting a defined contribution pension meant that your pot of money took a serious hit. If you had started to use your pension for a retirement income, or withdrawn a lump sum – or if you were aged over 75, and hadn't used your pot to purchase an annuity – a 55% tax charge was applied, before your beneficiaries could inherit your remaining fund.

That was a huge amount that your family would miss out on receiving; and significantly limited the usefulness of this pot of money in shaping their future. Yet since April of last year, this rule has been abolished.

Now, if you die before you reach 75, your beneficiaries will not have to pay any tax to receive your pension, or to make withdrawals from it (regardless of whether you had started to use it). They will receive every penny that is left over, and can spend it at will, tax-free. This assumes the benefits fall within the member available lifetime allowance (otherwise there would be a lifetime allowance charge).

If you die aged 75 or older, your beneficiaries can also inherit your pension tax-free, providing they leave the money inside the pension wrapper. They would then only have to pay income tax at their highest marginal rate when withdrawing from the fund. In other words, this would mean they could be exempt from paying any tax at all depending on their status. The only exception is if you die before this April, and are over 75, as a 45% tax rate will apply, on withdrawals, up until that point. Nevertheless, this is still more favourable than the old rule of 55%.

“ Now, if you die before you reach 75, your beneficiaries will not have to pay any tax to receive your pension, or to make withdrawals from it ”

This means you can leave your pension to your loved ones and they will pay little, if any, tax to receive and to use it. As your pension is not classed as part of your estate, it could also help if you have an inheritance tax liability (as it wouldn't be included when totalling up the value of your assets). So you now have a real opportunity to leave some, or all, of your pension to your loved ones in a tax-efficient way.

The tax treatment depends on the individual circumstances of the investor and may be subject to change in the future.





Time to take control

The 2015 pension freedoms have seen more people take up the option of keeping their pension fund invested in retirement, but doing so could require a different plan in the final few years of working.

With the stakes so high around saving up a pension, it is no surprise that many of us leave it in the hands of the experts, rather than managing it ourselves. What this means is letting our pension provider determine how and where to invest our savings, with the aim of growing its value further for when we need it.

Yet with the advent of the new pension freedoms, introduced last April, taking a greater interest in your pension, before retirement, is an increasingly important consideration.

The new rules have ended the requirement to use at least 75% of a defined contribution pension to arrange a retirement income, such as purchasing an annuity. It means that more people are keeping their pension fund invested in retirement (for example through income drawdown), and then taking an income or making withdrawals as and when they need to. In November 2015, the Association of British Insurers reported that, since the reforms, £2.85 billion has been invested into 43,800 drawdown products.

The advantage of keeping your pension invested, in retirement, is that this pot of money can potentially still grow in value, depending on the fortunes of the fund(s) it is invested into. This could result in a higher retirement income, and better standard of living, in your later years. That said, there are obvious risks to remaining invested, compared to the security of an annuity, such as if markets fall, this could have the effect of the retirement pot value falling too. Taking too much income could also significantly reduce the pot's value too quickly.

For this reason, it's important to regularly review your invested pension pot in retirement, potentially with the help of a financial adviser. That way, you can determine if it is performing in a way that suits your lifestyle and future goals – and perhaps, as you get older consider whether it might be appropriate to withdraw the remainder or trade it in for a guaranteed annuity income.

It's also important to pay greater attention to your pension pot before you retire. If your savings are currently being managed by your pension provider – such as through their default fund, or if you elected a life-styling approach – you need to make sure it continues to be positioned suitably for both the build up to, and point of, retiring.

This is because your pension provider may automatically start to reduce the level of risk your money is exposed to, as you get to 10 or five years away from your expected retirement date. This is done to protect your capital, and minimise the risk that you lose out if markets were to suddenly fall drastically, just before you retired.

Yet if you plan to remain invested in retirement, you might not want to reduce your level of risk in this way. Doing so could mean you miss out from market rallies, for example. If you are in a provider's default fund, it may also mean that your money is exposed to a lower level of risk than you would be prepared to take, and that you aren't achieving the growth you might be able to achieve from a higher risk fund.

[Sources]
<https://www.abi.org.uk/News/News-releases/2015/11/Pension-Stats-six-months-on>

The value of investments and the income from them can fall as well as rise and is not guaranteed. You may not get back the amount originally invested.

One careful owner

The Government has finally revealed details of its plan to help people who are trapped with a poor value annuity – but will they get a better deal?



Ignorance is not bliss for a generation of retirees. When it came to using their defined contribution pension to fund their retirement, many unwittingly agreed to an annuity deal that left them stuck on a low level of income.

Although annuities have had a bad press, the concept of the product is a sound one. In exchange for your pension savings, you receive a guaranteed level of income for as long as you live. Peace of mind and security. The problem is that rates had tumbled over the last 20 years; and some of the products were inflexible, failing to take into account the retiree's circumstances.

A 2014 study by the Financial Conduct Authority found that 80% of consumers who purchased their annuity from their existing provider could have found a better deal on the open market (where they shop around for a better deal). Nine out of ten consumers were not aware that they didn't have to stick with their provider.

The Government recognised this was a huge problem, and later that year announced they were abolishing the requirement for people to use their pension to arrange a retirement income. In other words, annuities are no longer compulsory. Great news, potentially, for future retirees; but what about people who were already retired, getting by on a reduced annuity income?

After a pledge to look into their plight, at the end of last year the Government finally released details of a second hand annuity market, launching in April

2017, which could help. Pensioners will be able to exchange their existing annuity deal for a cash lump sum, by selling it to someone else (such as an insurance company).

The annuity will continue to be paid to the third party, in line with however long the original annuity holder lives for.

If you have yet to retire and are considering taking out an annuity, you might also benefit from this new second hand annuity market. In other words, you may wish to consider the option of purchasing an annuity with your defined contribution pension from the age of 55, receive an income from it for a few years, and then potentially sell it later in life for a cash lump sum. Accessing pension benefits early is not suitable for everybody and is likely to reduce your income at retirement. It is important to carefully review your individual circumstances before making a decision.

With much of the detail behind how the second hand annuity market will work yet to be finalised, it is important for people considering this route to pay full attention to future developments, and to act with care.

One benefit of having an annuity, compared to keeping your pension fund invested, is that you don't have to be a financial expert. But the second hand annuity market could mean you have to become one – otherwise you risk receiving a worse deal than the annuity offer you originally agreed to.

[Sources]
<https://www.fca.org.uk/static/documents/thematic-reviews/tr14-02.pdf> and <http://www.dailymail.co.uk/money/pensions/article-3353955/Pensioners-pay-hefty-advice-fees-selling-unwanted-annuities.html>

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