Issue 8 Summer 2014

Financial Viewpoint

The Orchard Practice
0208 953 8687
info@orchardpractice.co.uk

Pensions reform No Lamborghinis here

In what's been described as the biggest ever shake-up of the UK pensions market, this year's Budget proposed major changes to how you access your pension savings when you retire.

In March, Chancellor George Osborne announced proposals for retirees to draw down as much or as little of their pension savings as they wished, at any time, with no caps or restrictions. These proposals have been subject to a consultation period, the outcome of which is expected during the summer.

If approved, you will have at least four options on how you access your pension savings from April 2015:

1 Full withdrawal from your pension

This option has grabbed all the headlines, especially since the Pensions Minister, Steve Webb, suggested people could spend all their pension savings on a new Lamborghini if they so wished. But this approach of cashing in most or all of your pension is unlikely to be the best option for most people.

Pension products attract significant tax advantages, so taking the money out without careful tax planning may result in a worse outcome for you. Under the new rules, the money you take out of your pension (above the 25% tax-free Pension Cash Lump Sum amount) would also be taxable as part of your income.

2 Take an annuity

Up until the Budget, this was the most popular option among retirees. The benefit of an annuity is that it provides the reassurance of a guaranteed income for the rest of your life. However, an annuity cannot be changed if your circumstances do and, if you die shortly after taking your annuity, it's often the pension annuity provider that benefits.

3 Drawing down your pension savings

This enables you to enjoy the tax benefits of a pension product, but with the flexibility to take out money as and when you need it (just like a bank account). You need to ensure you do not take out too much money in the early years, to avoid your money running out. Sound financial planning can help you manage your pension savings over time.

4 Combination of annuity and drawdown

This may be the ideal solution for many people. It enables you to secure a guaranteed level of income for the rest of your life to cover your main bills, while leaving the balance of your pension savings available for you to spend as and when you need it.

These changes offer much greater freedom, enabling you to control how you spend your money throughout your retirement years.

The Budget also revealed a number of changes that took effect from 27 March. If you are looking to take your pension benefits before April 2015, please contact us to find out if you can benefit from:

- the increased amount of total pension savings increasing from £18,000 to £30,000 (triviality limit) taken as a lump sum
- the limit on small pension pots being taken as a lump sum, increasing to £10,000 (from £2,000)
- the number of pots being increased to three (from two)
- the capped drawdown withdrawal limit being increased from 120% to 150% of an equivalent annuity
- the amount of guaranteed income you need in retirement to access flexible drawdown being reduced from £20,000 to £12,000

If you are aged over 55 and are considering taking your pension benefits, please get in touch to discuss your options.

Haircuts and homebuying:

New mortgage rules take effect

At the end of April, the Financial Conduct Authority (FCA) set out new rules that may make it harder for you to get a mortgage. All of your outgoings, including things like going out for dinner, travelling, childcare, and even the cost of a haircut, are now likely to be explored as part of the mortgage application process.

Advice moves centre stage

Advice is now mandatory in virtually all mortgage transactions, apart from where there's no dialogue between you and the lender (for example, if you complete an online application form and don't ask any questions along the way).

If you're used to getting advice from a mortgage adviser, you should only see a small change in this area, as most advisers already provided a fully advised service. This is not true, however, of many banks who often adopted a short, non-advised process. Overall, the changes will mean longer interviews and more detailed questioning on your circumstances and needs.

Affordability is paramount

The lender is now expected to undertake a detailed assessment to ensure you can afford the loan both now and in the future.

You should prepare for questions around the level of your 'non-discretionary' expenditure (eg. council tax, utility, childcare) as well as lifestyle expenditure (eg. entertainment, holidays and haircuts). You must also ensure your credit rating is as high as possible. As you get closer to applying for a mortgage, you should try to minimise lifestyle expenditure that could make the lender wary of your financial position.

Your adviser is likely to ask you for copies of recent bank statements. These will help them compile the information needed to submit your mortgage application to the most suitable lender. Your adviser will look for tell-tale signs of financial stress such as regular use of overdrafts, repayments of pay-day loans and other credit commitments, such as a car loan.

How plausible is your situation?

You should also expect your mortgage adviser to assess the plausibility of the picture painted by the information you provide. For example, is it likely that a couple, both working with two young children, have no childcare arrangements, or that the travel costs of a client are negligible when they work 100 miles from home?

A common sense approach

You should expect the process of taking out a mortgage to take longer. And where affordability is tight, some borrowers may find it harder to get a mortgage. But the new rules are common sense and should help ensure that only borrowers who can afford to repay their loan receive one.

If you want to discuss your circumstances, and how the new rules may affect you, please get in touch.

For arranging a mortgage a fee of £395 payable upon agreement to use our services.

YOUR HOME MAY BE REPOSSESSED IF YOU DO NOT KEEP UP REPAYMENTS ON YOUR MORTGAGE.

The Orchard Practice info@orchardpractice.co.uk 0208 953 8687

The towering tale of the IHT bill

The recent decision by one landowner to sell a family-owned mountain, to help settle a £9m tax bill, has highlighted the issue of Inheritance Tax (IHT) liability.

The Lake District's Saddleback Fell, otherwise known as Blencathra, has been put up for sale by its owner, Hugh Lowther, in an effort to raise money to meet a £9m Inheritance Tax (IHT) bill.

Mr Lowther inherited the mountain - and the bill - when his father, the 7th Earl of Lonsdale, died in 2006. However, a number of ongoing disputes and lengthy litigation have prohibited the family from raising the money required to pay off the bill, until now.

According to the HMRC rules that affect estates like the Lonsdale's, Mr Lowther now has just 18 months left to find the money. The mountain, which has been in the family's estate for around 400 years, is one of a number of assets they will be forced to sell.

IHT planning and you

Clearly, Mr Lowther's case is an extraordinary one, but it does highlight the importance of seeking ongoing, appropriate financial planning advice.

To find out if IHT planning should form part of your financial plan, please get in touch.

If you don't think this is something the average person should worry about, remember that the average UK house price is currently £253,000[1]. If you then start to add on your pensions, other investments and assets, it's easy to see how IHT planning may become an important part of your own everyday financial planning.

The current IHT rules allow the first £325,000[2] set against an estate to be tax free. If your spouse / civil partner dies first and passes their estate to you, it may be possible to double this allowance to £650,000. If, on your death, your estate is worth more than these thresholds, your loved ones could face a 40% tax bill.

Funding to meet an IHT liability on death is especially important where certain assets form an important and integral part of a family's heritage – as they do in Mr Lowther's case - and the intention is for this to continue.

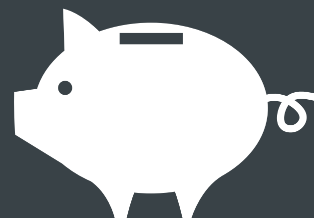
But regardless of whether you own a mountain, or something more modest, it's worth considering the impact IHT liability could have on you and your loved ones.

HM Revenue and Customs Practice and the law relating to taxation are complex, and subject to individual circumstances and changes which cannot be foreseen.

[1]Office of National Statistics

[2]www.hmrc.gov.uk/rates/iht-thresholds.htm

A NICER ISA



ISAs remain one of the most tax efficient solutions for your savings. On 1 July 2014, several restrictions were removed to improve flexibility and transfer options.

Under the so-called 'New ISA' (or NISA), Cash ISAs and Stocks and Shares ISAs have effectively been merged, with the overall limit increased to £15,000. This can be invested in either Cash, Stocks and Shares, or a mixture of both.

Previously, the combined limit was £11,880, of which a maximum of £5,940 could be invested in a Cash ISA (effective 1 April to 30 June 2014).

You'll also be able to transfer new and previous years' ISA investments from Stocks and Shares into Cash, and vice versa, as opposed to previous rules which restricted cash ISAs being transferred into Stock and Shares ISAs.

If you would like to discuss how you could maximise your ISA savings from 1 July 2014, or to find out how you could benefit from the new rules, please contact us.

The tax efficiency of ISAs is based on current rules. The current tax situation may not be maintained. The benefit of the tax treatment depends on the individual circumstances.

Make the most of Help to Buy

Help to Buy is in the news again. While no one knows exactly what's around the corner, even the Prime Minister has publicly admitted he would be prepared to amend the scheme if prompted to do so by the Bank of England governor, Mark Carney.

If you're considering using Help to Buy to realise your home ownership dreams, you may want to take advantage of the scheme before any changes are made to it.

What is Help to Buy?

Help to Buy is a government-funded initiative designed to help those who cannot otherwise afford to buy a home that meets their needs. The scheme comprises two parts:

1. **a 'mortgage guarantee', which helps you buy a home with a deposit of 5%. It's open to both first-time buyers and home movers for new-build and older homes in the UK with a purchase price up to £600,000**
2. **an 'equity loan', where the government will lend you up to 20% of the value of your newly-built home. Again, a minimum 5% deposit is required, and the maximum purchase price is £600,000**

For arranging a mortgage a fee of £395 payable upon agreement to use our services.

YOUR HOME MAY BE REPOSSESSED IF YOU DO NOT KEEP UP REPAYMENTS ON YOUR MORTGAGE.

Help to Buy and the housing market

Hardly a week goes by without Help to Buy making new headlines. With the scheme so closely linked with the housing market, there are opposing views on whether the scheme should stay or go.

All of the UK's main housing market indicators have registered an annual rise in property prices, with Nationwide reporting a 10.9% rise in the year to April 2014 – a trend many people attribute to the scheme.

Concerns over Help to Buy

Help to Buy was originally due to end in 2016, but was extended to 2020 in George Osborne's Budget. But there now seems to be a growing movement in favour of scaling it back.

While Help to Buy has made new-build properties more accessible for some buyers, and opened up the market for first-time buyers, there are fears it may cause a housing bubble and undermine affordability. A number of market commentators and economists, who blame Help to Buy for contributing to house price increases, have urged the government to make changes to the scheme.

To add fuel to the fire, the governor of the Bank of England, Mark Carney, has recently warned the Help to Buy scheme could distort the entire mortgage market and may have to be curbed. He has also expressed fears that allowing new home owners to secure a mortgage with a deposit of only 5% may be encouraging a return to risky lending. His remarks offer signs that the Bank of England may formally request a policy change in September.

The future of the scheme

If Help to Buy is scaled back, or withdrawn altogether, potential buyers may lose the advantage of being able to purchase a property with a smaller deposit than is ordinarily required. If that happens, expect to see a scramble from buyers looking to take advantage while the scheme remains in place.

If you're looking to take advantage of Help to Buy, please get in touch.

Independent report condemns 'hidden' 60% tax rate

The UK's leading independent economic research institute has criticised the complexity of current tax rules, particularly those exposing some higher earners to a 60% tax rate.

But if you're one of those affected by this tax anomaly, careful financial planning could help reduce your tax bill.

In its recent report, the Institute for Fiscal Studies (IFS) focused attention on a policy, introduced by the Labour government, that means those earning between £100,000 and £121,000 pay 60% tax on that part of their income.

The IFS also condemned the current government for failing to change the rules and missing the opportunity to simplify the tax system.

What is the 60% tax rate?

The 60% tax rate is caused by the gradual loss of the personal allowance between £100,000 and £121,000. Your personal allowance is progressively withdrawn at a rate of £1 for every £2 that your 'adjusted net income' is above the £100,000 income limit.

'Adjusted net income' is your total taxable income (salary, bonuses, certain taxable benefits, investment income and other income) minus certain tax reliefs.

Understanding the impact

The true impact of this is best illustrated by comparing the tax liability of one person with an adjusted net income of £100,000, and another whose is £120,000.

	Adjusted net income of **£100,000**	Adjusted net income of **£120,000**
Personal allowance (2014/15)	£10,000	£0
Taxable income	£90,000	£120,000
Tax payable	20% on £31,865 40% on £58,135 **Total tax payable: £29,627**	20% on £31,865 40% on £88,135 **Total tax payable: £41,627**

As you can see, the additional £20,000 of income attracts additional tax of £12,000, equating to an effective income tax rate of 60%.

How to reduce your tax liability

If you earn over £100,000, reducing your adjusted net income to £100,000 will help you retain the personal allowance and reduce the amount of tax you pay.

Pension contributions offer a simple way to achieve this.

Example

An individual has earned income of £130,000. As this is above £120,000, they would lose full entitlement to their personal allowance and pay tax of £45,627. If the same individual makes a pension contribution of £30,000 to a registered pension scheme via salary exchange, it would bring their adjusted net income down to £100,000. As a result, they would now pay tax of £29,627.

The individual would have retained their personal allowance and saved tax of £16,000.

Are you affected?

If you think you're impacted by this tax anomaly, you could benefit from a financial review. Even if you aren't affected, regular financial reviews can still help you make more of your money.

HM Revenue and Customs Practice and the law relating to taxation are complex, and subject to individual circumstances and changes which cannot be foreseen.

If you'd like to discuss changing your pension contributions, or want to arrange a financial review, please get in touch.

www.ifs.org.uk/publications/7203
www.ifs.org.uk/wps/wp201409.pdf

Risk versus reality

A new online risk calculator, from insurer LV=, uses UK morbidity and mortality statistics to identify your percentage risk of being off work for more than two months, suffering a serious illness, or dying before you reach retirement.

As an illustrative example, Jenny Jones is a 34 year-old non-smoker who plans to retire at 65. According to LV='s Risk Reality Calculator, Jenny has a:

- 46% risk of being unable to work for two months or more
- 13% risk of suffering a serious illness
- 6% risk of death

Perhaps the most striking result is that the likelihood of any of these things happening to Jenny before the age of 65 is 55%.

All the same, it won't happen to me…

Although the results are illustrative, the calculator highlights just how important one area of your financial planning – Life and Protection Insurance – really is. This becomes even more evident when you consider the reality of suffering a serious illness or dying suddenly:

- more than 1 in 3 people in the UK will be diagnosed with some form of cancer during their lifetime[1]
- cardiovascular disease causes around 74,000 premature deaths per year in the UK[2]
- we all face a 1 in 6 chance of having a stroke[3]

Ask yourself, how would your family cope if they couldn't rely on your income for a long period of time? Could they sustain their lifestyle if you were to die suddenly?

What's your risk profile?

If you would like to better understand your risk profile, please speak to us. We'll take a careful look at the impact this might have on your current circumstances, and help you identify any gaps in your existing protection arrangements.

Will my policy pay out?

If you're put off buying protection because you don't think it will pay out when you need it, think again. According to the Association of British Insurers £3.1bn was paid out on protection claims in 2013, the equivalent of 97% of all protection claims received during the year[4].

This meant that £8.4m was paid to 270 families every day last year, helping them to cope with the financial burden caused by long-term or serious illness and/or death.

To better understand your risk profile, or for a full protection review, please get in touch.

[1] Cancer Research UK, January 2014
[2] British Heart Foundation, Coronary Heart Disease Statistics 2014 (based on 2011 figures)
[3] World Stroke Organization - World Stroke Campaign, 2012/13
[4] www.abi.org.uk/News/News-releases/2014/05/Protection-Claims-2013-QA

Tips to prevent a DIY disaster

As the warmer weather arrives, more homeowners are likely to don the overalls and take on some household DIY.

But before you reach for the paintbrush or toolkit, it might be worth checking whether you're covered for any home improvement hiccups you might encounter.

DIY accidents cost the British public a staggering £1.5bn every year – that equates to an average of £280 per person. But despite the evidence that points to our accident-prone nature, a recent Paymentshield commissioned YouGov poll shows that more than a quarter of those questioned do not have basic home insurance cover in place.

Even basic cover could leave you exposed

If you have basic home insurance cover, you're already aware of the benefits it offers. But it's also important to ensure you have the appropriate optional extras in place with your policy.

For instance, Accidental Damage cover and Home Emergency cover are valuable additional benefits that cover you for certain mishaps that may occur at any time – but which are more likely to happen when you're undertaking home improvements.

If you would like help reviewing your insurance needs, please get in touch.

Protecting against a DIY disaster

We probably all have our own DIY disaster stories, which may include any one of the following:

- putting a foot through the ceiling while clearing out the loft
- drilling through a cable
- spilling paint on the carpet or tiles
- dropping a TV while trying to fix it to the wall

Accidental Damage cover can protect you against these common home-makeover mishaps. Similarly, Home Emergency cover can help protect you if your DIY activity results in something like an uncontrollable water leak, loss of power to your home or damage to your roof.

Don't botch your insurance cover

Putting adequate home insurance cover in place is a great start, but do take the time to check your policy to ensure it covers you for everything you need it to. If it doesn't, it may be wise to review your arrangements to ensure you're properly protected from potentially large, unexpected repair bills.

TIME TO REMORTGAGE?

After more than five years of the lowest interest rates in history, many of us are enjoying a period of low mortgage payments. But is that about to change?

After sustained signs of improvement in the UK economy, there's growing speculation that the Bank of England will soon increase the Base Rate from its current level of 0.5%. If and when that happens, there will be an impact on mortgage rates as lenders re-assess their standard variable rates and mortgage rates for new borrowers.

Seek professional advice

It's important to regularly review your mortgage, as it can often make sense to transfer to a new deal - or even a different lender. Your decision to transfer will depend on your individual circumstances, and the current rate you are paying. If your lender plans to increase its standard variable rate, moving to a new mortgage deal could save you money.

To discuss your remortgaging options, please get in touch.

For arranging a mortgage a fee of £395 payable upon agreement to use our services.

YOUR HOME MAY BE REPOSSESSED IF YOU DO NOT KEEP UP REPAYMENTS ON YOUR MORTGAGE.

The Orchard Practice
2 Penta Court, Station Road
Borehamwood
Hertfordshire
WD6 1SL

0208 953 8687
info@orchardpractice.co.uk
www.orchardpractice.co.uk

COPEN811 EXP 31/10/14