moneyworks

The essential consumer guide to making your money work harder.

Spring Edition

Inheritance tax planning: could your pension be the answer?

Rule changes to pensions make them a more attractive option for addressing a tax liability.

What next for interest rates?

The Bank of England has embarked on the first rate rise for a decade, but there remains a long way to go.

Don't fall off the retirement cliff

Failing to have sufficient pension plans in place could lead to significant financial headaches in retirement.

Five tax considerations for 2018

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Heaton Financial
Independent Financial Advisers Ltd

Welcome

A very warm welcome to the latest issue of **money**works and the first of 2018.

Last year saw the implications of Brexit weigh heavy on many people's minds and their savings and as we enter a new year, the long-term impact it will have remains uncertain.

However, in this edition of **money**works, we attempt to smooth the path by highlighting some of the big financial issues and what they mean to you and your money.

News that the 2018/19 tax year will introduce significant changes has left many wondering what impact it will have on their savings and investments, and in this issue, we look at five key areas you should consider under the new rules.

With inflation reaching a six-year high and interest rates remaining dismally low for savers, we look at why now might be the right time to re-evaluate your long-term financial plans.

We also take a look at the complexities surrounding inheritance tax and how despite the introduction of favourable new rules last April, the amount collected by the government is still at record highs. In this issue we ask if rule changes to pensions could make them a more attractive option for addressing a tax liability.

Finally, we look at the importance of having sufficient pension plans in place and how you can avoid significant financial headaches in the future by addressing the issue now.

Here's wishing you all a very prosperous New Year and we look forward to bringing you more regular updates over the coming year.

Best wishes

The **money**works team

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The 2018/19 tax year heralds the introduction of tax changes that might impact on your savings and investments. Whilst despite industry speculation, other rules remain the same.

The News in Brief

A round-up of the current financial stories.

How big is your pension pot?

The average UK worker will need to build more than £300,000 into a pension to maintain their current lifestyle in retirement, according to January 2018 research by Aegon.

This figure is based on the average UK employee earnings of £27,000, as revealed by the government as part of its auto-enrolment review announced in December. The government also believes we should be targeting a retirement income equivalent to two-thirds of our working income – £18,000 a year, or £1,500 a month.

So an average earner, who would be entitled to £691 state pension a month, would need to generate a monthly income of £809 from their own private pension pots to meet this target.

Source:

https://www.ftadviser.com/retirement-income/2018/01/04/savers-told-they-need-300k-pension-pot-to-retire-well/

The (rising) age of inheritance

When you're struggling to achieve life's major goals, such as getting onto the property ladder, the windfall of receiving an inheritance could make all the difference.

However, a December 2017 report by the Resolution Foundation has found that people currently aged between 25-35 – known as millennials – will have to wait until they are nearly at retirement age for their inheritance.

The research found that, on average, millennials will be 61 before they receive an inheritance. When the older generations' estates are eventually passed on, the good news for millennials is they're likely to receive larger levels of wealth. The Resolution Foundation states that inheritances are set to double over the next two decades, peaking in 2035.

Source:

http://www.resolutionfoundation.org/media/press-releases/millennials-are-set-for-an-inheritance-boom-but-it-wont-solve-their-home-ownership-and-inequality-woes/

Cost of moving house reaches record high

Moving house is considered to be the most stressful life event you can experience – and it will also prove very expensive.

December 2017 research by reallymoving.com concluded the average cost of moving house has reached a record high of £7,381. 44% of the total cost of moving is made up of estate agent fees (averaging £3,254), followed by stamp duty (27% of the total amount), with other outgoings including conveyancing fees and removals.

As ever with the housing market, there are stark regional differences in costs. In London, for example, the average outlay for moving home is a considerable £23,913.

Sources:

https://www.express.co.uk/news/uk/574171/Divorce-stressful-moving-home

https://www.reallymoving.com/blog/december-2017/uk-cost-of-moving-reaches-record-high

The cost of no financial advice

November 2017 research from Nottingham Building Society has found that – with the support of financial advice – better savings habits can be developed.

On average, Nottingham discovered people put £1,600 less away every year when they don't have access to financial advice. One in five of us say they are saving less because they're unable to find suitable financial advice on how to properly handle their money. 21% admit they don't think they're saving as much as they should.

Amongst those who aren't receiving financial advice, they believe they'd be able to put aside an average of £134 a month for their future – which works out at more than £1,600 in lost savings every year.

Source:

https://moneyfacts.co.uk/news/savings/savers-lose-out-on-1600-without-advice/

Inheritance tax planning: could your pension be the answer?

Rule changes to pensions make them a more attractive option for addressing a tax liability.

The issue of inheritance tax continues to grow. Despite the introduction of favourable new rules last April, the amount of inheritance tax collected by the government has reached record high levels and is forecasted to keep rising over the next five years.

If, when you die, the value of your estate falls above your personal inheritance tax threshold (the highest amounts being up to £450,000 if you're single or divorced, or up to £900,000 if you're married or widowed, for the 2018/19 tax year), everything you own above it will be taxed at 40%. Typically, it will fall on your family to settle this tax bill, which can often run into thousands of pounds.

There are different ways you can address an inheritance tax liability, and – thanks to rule changes – your pension might be the answer.

Special status

The way HMRC calculates a potential inheritance tax liability is to add up the value of the deceased's estate.
This includes your property, car, savings and investments.

But, crucially, not pensions. If you've a defined contribution pension, it has special status that allows it be passed on without it forming part of your estate. This is not a new development, but what has changed are the rules around inheriting defined contribution pensions – and here is where the opportunity lies.

Before the 2015 pension freedoms, if you died over the age of 75, or after taking money from your plan, your remaining pot could only be passed to loved ones after incurring a 55% tax charge. This has now been scrapped. If you die before you're 75, your family can inherit your pension tax-free. If you die after 75, they will only have to pay tax at their highest marginal tax rate, rather than 55%, to receive these funds.

The fact it isn't part of your estate means you can, in theory, have up to £1,030,000 in a defined contribution pension (for the 2018/19 tax year), and it can be passed on to your family without incurring inheritance tax or any lifetime allowance charges. There may still be tax to pay, if you're over 75, but it could work out much lower.

Planning your future

When it comes to funding your retirement, these significant changes to inheriting pensions could influence how you use your different savings.

For example, if you have savings and investments not held in a pension wrapper, it might prove more tax-efficient to use these for a retirement income. After all, there are tax implications for withdrawing from your pension, beyond the 25% tax-free element. Withdrawing from your savings and investments could prove more tax-efficient.

One of the key tax advantages of not touching your pension until a last resort is that, compared to other investments such as ISAs, Collectives and Bonds which would all be included in the deceased's estate for IHT, it will maximise the amount that can potentially be passed down to your loved ones tax free.

Therefore, when it comes to your family's inheritance – and if your estate could trigger an inheritance tax liability – you might find using your pension is the most effective way of passing on your wealth to loved ones.

A financial adviser can look at your situation and long-term plans, to advise you of the most tax-efficient way of using your savings to fund your future – and beyond. They can help you consider if inheritance tax might be an issue to plan for, and outline your options.

Levels and bases of and reliefs from taxation are subject to change and their value depends on the individual circumstances of the investor. The Financial Conduct Authority does not regulate taxation & trust advice.

(Sources: https://www.which.co.uk/news/2017/06/inheritance-tax-bills-top-5-billion-for-first-time/
https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/661480/autumn_budget_2017_web.pdf)

What next for interest rates?

The Bank of England has embarked on the first rate rise for a decade, but there remains a long way to go.

The pain goes on for savers. Despite the Bank of England increasing interest rates from 0.25% to 0.5% in November, interest rates on savings accounts remain at dismally low levels, with no end in sight. With inflation reaching a six-year high in the same month, growing your savings in real terms remains a considerable challenge.

Certainly, the rate rise failed to deliver the upturn in savings rates many hoped. December 2017 research by Moneyfacts found the number of savings accounts paying a higher rate than 0.5% fell by 150 in the month that followed the base rate rise – the biggest drop in almost a decade.

The average easy access account rate crept up by just 0.06% to stand at 0.45% – showing banks and building societies were failing to pass on the full benefit of the base rate rise.

According to figures from the Building Societies Association, in November 2017, the average bank and building society savings instant account was paying just 0.12%, including bonus. The average one-year fixed rate bond offered just 0.72%. Back in July 2016 – just after the EU Referendum and before the decision to reduce base rate to 0.25% – these accounts were paying an average 0.34% and 0.93% respectively. In other words, average rates remain worse now than before the last rate cut.

Slow progress

The Bank of England's first rate rise since the global financial crisis was a clear signal of its growing confidence in the UK economy, following the initial uncertainty over Brexit. But savers hoping it would be followed up by further rate rises – such as the US has experienced – have been disappointed. That seems to be it, for the near future at least.

Speaking in January 2018, Bank of England policymaker Silvana Tenreyro expects two further increases in base rate would be needed over the following three years, but that the Bank had "ample time" before considering the next rise. This view mirrors the governor Mark Carney, and other senior officials at the Bank. Economists themselves are divided over the prospects for 2018, with a Financial Times survey finding one-fifth of economists believe there will be no increase, whilst two-fifths expect it to rise by at least 0.5%.

But whatever happens in the near future, one simple truth will remain unaltered for savers. It is going to be a long time, if, indeed, ever, before interest rates return to the 5%+ levels seen in 2007.

Re-evaluating your long-term plans

Savings accounts will always play a part in a sensible investor's portfolio. The security, and ease of access, makes them ideally suited for your short-term financial needs.

Yet when it comes to your long-term financial priorities, the personal finances world has simply changed. Savings accounts are no longer able to generate meaningful, life-altering returns. If you have money ear-marked for your future and are prepared to commit it for the long-term, other options need to be considered.

Investing your money offers the potential to achieve higher returns. You will need to accept risk to your capital, but speaking to a financial adviser can help to develop an investment strategy that's right for your needs.

The value of your investment can go down as well as up and you may not get back the full amount invested. Investments do not include the same security of capital which is afforded with a deposit account.

(Sources: http://www.bbc.co.uk/news/business-42320052
https://moneyfacts.co.uk/news/savings/base-rate-beating-savings-deals-fall-sharply/
https://www.bsa.org.uk/statistics/savings
https://www.reuters.com/article/us-britain-boe-tenreyro/ample-time-before-next-bank-of-england-rate-move-needed-tenreyro-idUSKBN1F42EZ?il=0)

Don’t fall off the retirement cliff.

Failing to have sufficient pension plans in place could lead to significant financial headaches in retirement.

An over-reliance on the state pension could prove dangerous. The £8,456.20 maximum amount of annual income it pays, for the 2018/19 tax year, is certainly an extremely valuable benefit to support your lifestyle. But on its own, will it be enough to provide for your retirement?

A December 2017 report, by the Organisation for Economic Co-operation and Development (OECD), suggests it won’t. The report warns many people could face something of a retirement income cliff – because the gap between UK employment earnings and state pension income is the largest in the developed world.

On average, state pension income equates to around 29% of what UK people earn – or less than a third of the income you currently receive. This compares unfavourably to other developed nations, where state retirement income is an average of 63% of earnings.

So if you want to maintain or enhance your lifestyle, you face a huge shortfall to make up.

The importance of planning

Understandably, many of us feel apprehensive about our retirement plans. June 2017 figures from the Office for National Statistics show 46% of working adults, who were questioned between June and December 2016, aren’t confident their retirement income will give them the standard of living they hope for. Over two-thirds have not thought how long they will need to fund retirement for. The last point is important. Thanks to improvements in living standards, people are living longer and your retirement plans need to factor this in. It’s not just about having savings for the first few years of retiring, but considering how your needs might change, and if you might require provisions for areas like long-term care.

There’s also your family’s inheritance. You may want to leave some of your wealth behind for them to enjoy, rather than spending all of it to fund your retirement.

Are you paying enough into a pension?

It’s never too early to start preparing for retirement, so if you have a few years left of working, considering your current arrangements could allow you to make better plans.

For example, you might want to pay more into your pension, or even set up additional pensions. A huge advantage of taking this route is tax relief, as the government tops up your contributions by 20% or 40% (depending on if you’re a basic or higher rate taxpayer). With the pension freedoms also opening up your options for using these savings, from 55, you have greater flexibility to shape your retirement. There are important tax considerations around making withdrawals.

The way your pension contributions are invested is another key factor. If you’re enrolled in your employer’s default pension scheme, there’s every chance it’s invested in a way that’s not fully suited to your circumstances. You might be willing to take more risk with your money, for example.

With the stakes so high, speaking to a financial adviser is recommended. They can help you consider what you want to achieve in retirement, and if you have the provisions to make it happen.

Retirement should be a chapter in life to relish, but it’s a leap into the unknown. A financial adviser can help you to plan for different scenarios, so you can look forward with confidence.

The value of your investment can go down as well as up and you may not get back the full amount invested. Accessing pension benefits early may impact on levels of retirement income and is not suitable for everyone. You should seek advice to understand your options at retirement. Levels and bases of and reliefs from taxation are subject to change and their value depends on the individual circumstances of the investor.

(Sources: http://www.thisismoney.co.uk/money/pensions/article-5147989/OECD-report-puts-Britain-bottom-pension-league-table.html

https://www.ons.gov.uk/peoplepopulationandcommunity/personalandhouseholdfinances/incomeandwealth/articles/earlyindicatorestimatesfromthewealthandassetssurvey/attitudestowardssavingforretirementautoenrollmentintooccupationalpensionscreditcommitmentsanddebtburdenjuly2016todec2016)

Five tax considerations for 2018.

The 2018/19 tax year heralds the introduction of tax changes that might impact on your savings and investments. Whilst despite industry speculation, other rules remain the same.

1) How much you can pay into a pension over your life

The lifetime allowance – which limits how much your total pensions can grow to, without paying tax – is being increased from £1 million to £1,030,000. This 3% rise is a welcome boost for many people. For example, more than 2,500 people exceeded their lifetime allowance over the 2016/17 tax year, triggering an average tax bill of £46,332.

As recently as 2011/12, the lifetime allowance was £1.8 million before it was significantly reduced. This trend is now starting to be reversed, meaning you can build up more in your pension.

2) How much you can pay into a pension, once you start to use it

Since the 2015 pension freedoms were introduced, you can withdraw from your pot whilst still paying in. However, the annual amount you can continue to save, after you take up one of the pension flexibility options, changed last April.

Known as the Money Purchase Annual Allowance, the annual tax-free allowance has reduced from £10,000 a year to just £4,000. In other words, if you've started using your pension, but intend to keep paying in, you and your employer can now only save £4,000 a year.

3) The level of tax relief you can receive through pension contributions

In the run-up to recent Budget announcements, rumours of government plans to scale back favourable tax relief rules have circled. However, last November's Budget once again saw no changes.

This means you can continue to benefit from 20% (if you're a basic rate taxpayer) or 40% (if you're a higher rate taxpayer) tax relief on your pension contributions. Over time, this can make a considerable difference.

In the long-term, there are still doubts about the viability of this tax perk. For the 2015/16 tax year, the government spent more than £50 billion on tax relief, which eventually may prove unsustainable.

4) The amount you can receive in dividends

The amount of dividends you can earn from your investments – without paying tax – is being reduced from £5,000 to £2,000 a year.

So if you have investments that generate dividends above £2,000, you'll have to pay tax at a rate of either 7.5%, 32.5% or 38.1% – depending on your tax position. This doesn't apply to investments held within an ISA.

5) The amount you can save or invest into an ISA

The ISA allowance for the 2018/19 tax year has been frozen at £20,000, but this still remains a hugely valuable benefit. With no tax to pay on any returns from money held in an ISA wrapper, it makes sense to consider using your new allowance when the tax year begins.

Looking for help minimising tax?

The level of tax you pay can make a huge difference to your overall wealth, so it can really pay off to make sure your savings and investments are as tax-efficient as possible. This is something a financial adviser can support you with. By reviewing your current plans, they can identify ways of reducing the amount of tax you have to pay.

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The value of your investment can go down as well as up and you may not get back the full amount invested. Accessing pension benefits early may impact on levels of retirement income and is not suitable for everyone. You should seek financial advice to understand your options at retirement. Levels and bases of and reliefs from taxation are subject to change and their value depends on the individual circumstances of the investor.

(Sources: http://www.telegraph.co.uk/pensions-retirement/tax-retirement/46332-average-tax-bill-people-saved-much-pension/
https://www.moneywise.co.uk/pensions/retirement-lifestyle/beat-the-1m-lifetime-allowance-pensions
http://citywire.co.uk/money/fears-of-cut-to-pension-tax-relief-as-bill-hits-50bn/a1056794)

And finally....

Have you lost track of your pensions?

January 2018 figures from the government have revealed a staggering £400 million is currently sat in unclaimed pension savings, due to millions of savers losing track of old pensions.

Previously, the government revealed the average worker switches jobs 11 times over their career. A change of employer can often lead to starting up a new pension, and – for many it seems – forgetting about the old ones.

The latest government research discovered that a fifth of us have no idea how to track old pension pots down. If you do have older pensions, these pots of money could play an important role in your future – and it's a good idea to review them to see if they're suitably positioned to support your retirement goals.

The government operates a pension tracing service, to help you find lost pensions (visit: www.gov.uk/find-pension-contact-details).

Sources:

https://www.express.co.uk/finance/personalfinance/898886/pensions-millions-unclaimed-savings

http://www.thisismoney.co.uk/money/pensions/article-4644230/Is-worth-combining-pensions-one.html

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