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Financial Viewpoint

Your latest newsletter from Eureka Financial Solutions

EUREKA FINANCIALSOLUTIONS®

Investing for the next generation

"A good start in life" is what all parents want for their young children.

Initially this often translates into a surplus of toys but, give or take technology fads, this stage eventually passes. At that point thoughts turn towards the future and the transition from child to adulthood.

The longer-term perspective raises the possibility of making investments for your children which they can call on in adult life. This can lead to a variety of issues:

- are there particular needs which should be targeted or is flexibility more important?
- which investments would be appropriate?
- can some parental or other controls over when children can have access to the investment be put in place?
- which are the most tax efficient?

Save for what?

For today's children, the path through the early years of adulthood looks rather different from, and more expensive than, that of parents and grandparents:

Higher education may be seen to be more important for getting that dream job but it also comes at a much higher cost. Taking into account tuition fees, accommodation and living expenses, a three year degree is likely to cost students between £35,000 to £40,000. Before 1998, there were only grants. Loans for tuition fees did not begin until 2006. You may have left university with a bank overdraft, but the sum owing probably pales into insignificance compared to the five figure debts many of the coming generations of graduates face.

Marriage can be costly for those who choose it. According to the consumer website Money Saving Expert, the average wedding costs around £20,000. One third of couples questioned admitted going into debt to pay for their wedding.

Getting on the first rung of the **property ladder** is another growing cost for the next generation. The typical first-time buyer borrows over 3.39 times their income with a deposit of 17% and we've all heard of the Bank of Mum and Dad.

Once they have the degree, the job and the home (and the mountain of debt), there's another long-term financing requirement which today's children will encounter: retirement provision. The final salary pension scheme, which has benefitted today's retirees, has virtually disappeared for new private sector employees.

Take expert advice

Two principles that apply to many aspects of financial planning are particularly relevant when thinking about children:

1. The sooner you start the better, and the more scope there is for investments to grow (although there's still no guarantee that they will).
2. Take expert advice before making any decisions. The right investment set up in the wrong way can be worse than the wrong investment set up in the right way.

The value of your investments and any income from them can fall as well as rise and you may not get back the original amount invested.

If you want to help your child progress through this financial landscape, please get in touch.

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At retirement: the runners and riders

With the much-lauded pension freedoms, we now have a range of options when deciding how to fund our retirement.

Whilst many newspaper headlines warned that new retirees would blow their entire pensions savings on Lamborghinis, it appears that most have taken a more measured approach. Data from the Association of British Insurers (ABI) shows that in the first year following their introduction 57% of new retirees took less than 1% of their pot and fewer than 4% of retirees took out more than 10%. The majority of these were in the first few months following the changes.

But not everyone is affected by the new freedoms.

Those who are, or have been, members of a final salary/defined benefit scheme **won't be affected by the new regulations**. These schemes provide a pension based on your years of service and your salary when you left the scheme, or, if it is no longer operating, the point at which it closed.

Those with a defined contribution scheme – or who have made additional contributions into a free-standing pension plan – **will benefit from the new freedoms**. You can buy an annuity, draw income from your savings, or withdraw lump sums as you need them.

Annuities

Buying an annuity is the traditional means of converting your savings to a guaranteed income stream. This could include an income for your spouse on your death and/or inflation proofing. However, annuities have had a bad press in recent years as the returns on bonds – the investments that underpin the income stream – have collapsed. This has made them seem poor value for money.

Flexi-Access Drawdown

You can elect to remain invested and withdraw income from your pension savings. However, the income from investments is variable and the value of the underlying investments may vary over time.

Uncrystallised Pension Fund Lump Sums

This rather inelegant term describe, a newly-introduced freedom. If you have more than one defined contribution scheme and one that you have not touched (ie. elected to buy an annuity or elected to withdraw income), you can use it to 'top-up' your retirement by taking occasional lump sums.

Horses for courses

The table below summarises the key features of the three options now available to retirees. With options comes choice, and choices can be hard to make – particularly in an area as important as your pension.

The likelihood is that those retiring today will have a combination of income sources at their fingertips: the State Pension, an element of defined benefit and an element of defined contribution. Some may elect to continue working in a part-time or advisory capacity or on a consultancy basis.

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

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

This will be one of the most important decisions of your life as it determines the kind of retirement you can afford. Further, managing your tax liabilities when you have more than one source of income open to you can be complicated. The right solution for you will depend on many variables, so please do get in touch before making any decisions.

	Annuity	Drawdown	Lump sums
Guaranteed income	Yes	No	No
Up-front tax-free lump sum	25%	25%	N/A
Additional withdrawals	No	Subject to normal personal income tax rules	25% tax free The remainder subject to personal income tax rules
Death before 75	Spouse's annuity paid tax free	Tax free lump sum or Tax free drawdown	Tax free lump sum or Tax free drawdown
Death after 75	Spouse's annuity taxed as income	Lump sum taxed at highest marginal rate Drawdown subject to normal income tax rule	Lump sum taxed at highest marginal rate Drawdown subject to normal income tax rules

OW0437 Exp. 31/03/17

Saving for retirement: as easy as 1, 2, 3

Much is made of the tax benefits of saving into a pension scheme but there are other benefits to consider.

As many corporate pension schemes and even government pension schemes become unsustainable, the onus to create a comfortable retirement is increasingly on the individual. But, if we are honest with ourselves, by the time many of us start thinking about our pensions it can feel daunting.

Here are our top tips for a more comfortable retirement:

1. Start early

Starting early cannot be stressed enough and is probably the most important piece of advice we can give. Investing even small amounts can make a significant difference to the potential outcomes as you can see below:

Age when saving starts	Amount to save per month	Total saved by age 67
21	£20	£11,280
30	£25	£11,400
40	£33	£11,200
50	£52	£11,250
60	£117	£11,232

Even if finding £20 a month is difficult at 21, it could be a lot easier to find than £117 a month at 60.

The figures above show saving without investing the money. Any money you invest at age 21 will have accumulated 46 years of returns by the time you come to retire; anything invested from 45 has only 22 years.

2. Join your employer's scheme

Following the introduction of auto-enrolment all employers must now offer their employees a workplace pension scheme, although not all employees are required to join. However, by joining the scheme, not only will you be contributing to your future comfort but your employer contributes too, boosting the total potential returns. This is particularly important if you think you might have a career break at some point in your working life, for example to have a family.

Most schemes employ a 'salary sacrifice' model where your contributions are deducted before tax is calculated, making it a simple way to save. If your employer doesn't offer this kind of scheme, speak to us about setting up a personal pension plan. These non-employer sponsored schemes will assume you are a basic rate tax payer and calculate your contributions net of basic rate tax (so if you want to put aside £100 a month, your contributions will be £80 and the scheme will claim the additional £20 from HMRC). If you're a higher rate tax payer you will need to claim the additional tax back through your self assessment tax form.

If you're self-employed, a contractor or have irregular income, consider a Self Invested Personal Pension (SIPP).

3. Top it up

Many schemes allow you to make additional contributions and some employers will match these to a maximum percentage of your salary. You can still invest more but the employer's matching contribution will be capped. Alternatively, if your employer offers an Additional Voluntary Contributions (AVC) scheme, consider signing up for this. They won't contribute to it but, again, saving even a small amount into the plan can help over the longer term.

Under current guidelines anyone not drawing a pension can invest up to £40,000 of their taxable income into their pension scheme(s) tax free per tax year unless their total pension savings exceed the lifetime allowance (currently £1,000,000). And remember, using an ISA can increase your tax-efficient savings.

Conclusion

So there we are. Starting as early as you can gives you the benefit of time; joining an employer's scheme makes saving simple and boosts your savings rate; and investing as much as you can afford can maximise the tax benefits.

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 are concerned in any way about preparing for your retirement, speak to us about the options available to you.

OW0473 Exp. 31/03/17

Maximise your ISA allowance

If you haven't used up your Individual Savings Account (ISA) allowance for 2016/17, you have until 5 April to do so.

Saving into an ISA is a great way of making your savings work harder. Whether you're looking to supplement your retirement income, build up funds for a property purchase or you simply want a 'rainy day' nest egg, ISAs offer an array of tax-efficient savings options. But with the tax-year end fast approaching, the clock is ticking for you to use your full 2016/17 ISA allowance of £15,240.

Why is it so important to use up your allowance? Here are some great reasons:

Your ISA is tax-efficient

Unlike some other investments, your returns are not subject to tax. That means every extra pound you save (within your allowance) will be sheltered from the taxman. This tax year, you can invest up to £15,240 tax-free.

You can't 'carry over' your ISA allowance

You cannot carry any unused ISA allowance over to the following tax year unlike some other personal allowances (such as your pension annual allowance). That makes it doubly important to invest your full allowance, if you can afford to. You also have the freedom to take money out and put it back in later in the same tax year, without losing any of your tax-free entitlement. That means you needn't worry about missing out on lost interest if you need to make a short-term raid on your savings, but can afford to replace it later.

The miracle of compound interest

Maximising your ISA savings can deliver huge benefits over the longer term. For instance, assume you invested the current maximum allowance of £15,240 in a Cash ISA, every year, for 25 years. Even if your investment grows at a modest 2.5% each year, your investment would have grown to £555,841.15.

Inheriting an ISA

Before April 2015, any savings held in an ISA automatically lost their tax-free status on the death of the ISA holder. Since April 2015, however, the Additional Permitted Subscription allows the spouse / partner to retain the tax benefits in the form of a one-off ISA allowance equal to the value of the ISA at the date of the holder's death. For example, if your partner had £40,000 in ISA savings including interest, your ISA allowance for that tax year would be £55,240 (the value of your partner's savings and your own ISA allowance for the 2016/17 tax year).

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. The value of your stocks and shares ISA and any income from it may fall as well as rise. You may not get back the amount you originally invested.

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TO OPEN AN ISA, YOU MUST BE:

- 16 or over (for a cash ISA)
- 18 or over (for a stocks and shares ISA)
- Resident in the UK
- A Crown servant (eg. diplomatic or overseas civil service) or their spouse or civil partner if you don't live in the UK

Contact us for more information or advice about the different kinds of ISA investments. We will help you to make the best choice for you and your family.

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